THE BULGARIAN ECONOMY

OCTOBER 2005

REPORT BY

THE CENTER FOR ECONOMIC DEVELOPMENT

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The Center for Economic Development (CED) is a Bulgarian non-governmental research institute in the area of economic policy, established in 1997. Its goal is to support the economic development of Bulgaria through encouragement of public debate on economic issues and development of economic policy options.

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ABBREVIATIONS USED

AASEWA .... ACT AMENDING AND SUPPLEMENTING THE ENVIRONMENT AND WATERS ACT
ASIFC .... AGENCY FOR STATE INTERNAL FINANCIAL CONTROL
BEIA.......................... BULGARIAN EXPORT INSURANCE AGENCY
BNB .... BULGARIAN NATIONAL BANK
BSP .... BULGARIAN SOCIALIST PARTY
BTC .... BULGARIAN TELECOMMUNICATIONS COMPANY
CED .... CENTER FOR ECONOMIC DEVELOPMENT
CoM .... COUNCIL OF MINISTERS
CPC .... CRIMINAL PROCEDURE CODE
CPI............................ CONSUMER PRICE INDEX
CRC .... COMMUNICATIONS REGULATION COMMISSION
DCM .... DECREE OF THE COUNCIL OF MINISTERS
EC............................. EUROPEAN COMMISSION
EDC .... ELECTRICITY DISTRIBUTION COMPANY
EFTA......................... EUROPEAN FREE TRADE ASSOCIATION
EU............................ EUROPEAN UNION
EWA.......................... ENVIRONMENT AND WATERS ACT
FSC .... FINANCIAL SUPERVISION COMMISSION
GDP.......................... GROSS DOMESTIC PRODUCT
GVA .... GROSS VALUE ADDED
HACCP .... HAZARD ANALYSIS AND CRITICAL CONTROL POINT SYSTEM
ICT............................ INFORMATION AND COMMUNICATIONS TECHNOLOGY
IMF .... INTERNATIONAL MONETARY FUND
ISCRASP.................. INTEGRATED SYSTEM FOR CIVIL REGISTRATION AND ADMINISTRATIVE SERVICE OF THE POPULATION
JSC........................... JOINT STOCK COMPANY
MEW......................... MINISTRY OF ENVIRONMENT AND WATERS
MF .... MINISTRY OF FINANCE
MH............................ MINISTRY OF HEALTH
MI.............................. MINISTRY OF ECONOMY
MRF .... MOVEMENT FOR RIGHTS AND FREEDOMS
MV .... MOTOR VEHICLE
NA............................. NATIONAL ASSEMBLY
NAMRB..................... NATIONAL ASSOCIATION OF MUNICIPALITIES IN THE REPUBLIC OF BULGARIA
NDP .... NATIONAL DEVELOPMENT PLAN
NEC .... NATIONAL ELECTRICITY COMPANY
NFI............................ NON-FINANCIAL INSTITUTION
NMSII........................ NATIONAL MOVEMENT SIMEON II
NPP .... NUCLEAR POWER PLANT
NRA .... NATIONAL REVENUES AGENCY
NSI............................ NATIONAL STATISTICAL INSTITUTE
NSSI .... NATIONAL SOCIAL SECURITY INSTITUTE
OECD .... ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT
OG............................ OFFICIAL GAZETTE
OPF .... OCCUPATIONAL PENSION FUND
PA .... PRIVATIZATION AGENCY
PIC............................ PENSION INSURANCE COMPANY
POSA........................ PUBLIC OFFERING OF SECURITIES ACT
PPA........................... PUBLIC PROCUREMENT ACT
PPP .... PUBLIC-PRIVATE PARTNERSHIP
PPR .... PUBLIC PROCUREMENT REGISTER
RIEW .... REGIONAL INSPECTORATE OF ENVIRONMENT AND WATERS
SAITC .... STATE AGENCY FOR INFORMATION TECHNOLOGY AND COMMUNICATIONS
SEWRC .... STATE ENERGY AND WATER REGULATORY COMMISSION

ABBREVIATIONS USED

SIPJSC .... SPECIAL INVESTMENT PURPOSE JOINT STOCK COMPANY
SME .... SMALL AND MEDIUM-SIZED ENTERPRISES
SOJSC .... SINGLE OWNER JOINT STOCK COMPANY
SPC .... SUPREME PROSECUTOR'S CASSATION
SSS .... STATE SOCIAL SECURITY
TIPC .... TAX INSURANCE PROCEDURE CODE
UN .... UNITED NATIONS ORGANIZATION
UPF .... UNIVERSAL PENSION FUND
VAT .... VALUE ADDED TAX
VPF .... VOLUNTARY PENSION FUND

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SUMMARY

The Bulgarian economy continues its development at a high pace. The business climate remains favorable but the Estat index of business climate indicates delayed upward trend of economic growth and we expect lower growth for the second half of 2005. CED estimates annual economic growth at 5.7-5.9 per cent.

Growth in industry accelerates while growth in construction registers slight delay. Investments in the economy increase significantly, partly because of Government's extra capital expenditures in the second quarter. Growth in labor productivity measured as the value added per one employed is higher than growth in employment, which stops the unfavorable trend of last year.

The current account deficit, which is generally a result of the increasing trade deficit, remains a major macroeconomic problem. The share of investment goods in imports goes up thus confirming the thesis that the trade deficit is a natural result of the high amount of domestic and foreign investments and should not be assessed as completely negative.

Despite the delay in the privatization process, foreign investments register dynamic growth and will exceed EUR 2 m this year. This guarantees stable balance of payments and currency board.

In the third quarter of 2005, banks overcame BNB's March and April regulations and credit expansion continued at a pace close to the record-breaking levels of last year. After a dull summer, capital markets register a smooth upward trend.

In the public finance sphere, the tendency to realize growing budget surpluses has aggravated. Intentions to lower the tax and social security burden actually transfer this burden from direct to indirect taxes but do not lower it noticeably.

In a sectoral perspective, highest growth dynamics register the processing industry, tourism and telecommunications. Transport and agriculture register delay, especially following floods-generated losses.

The new Government has not formulated yet its economic policy in sufficiently clear terms.

Our projections for **rather high economic growth** in the second quarter above the values for the first quarter are confirmed by NSI's preliminary data showing growth at 6.4 per cent. According to our projections, total economic growth will remain at rather high levels but growth in the third quarter will register delay, reaching levels of 5.6 - 5.8 per cent compared to previous values. Overall, for 2005 we expect higher growth compared to that in 2004 (5.6 per cent), within the 5.7 - 5.9 per cent range. Services have the highest share in economic growth in terms of supply and exports have the highest share in terms of demand. Industry and investments register the highest dynamics, with growth in industry and services going up against the second quarter of last year. Growth in industry intensified compared to the previous quarter whereas growth in services registered delay. Decline in agriculture intensified again.

Value added growth in industry registers the highest values and stands at 9.3 per cent. The processing industry registers accelerated growth of 11.5 per cent with a share of 2 percentage points in GDP growth. While growth in construction delays compared to the previous quarter, it still has the highest share of 13.8 per cent. We expect for growth in industry to remain at high levels, but it will hardly continue at accelerated pace. Growth in construction will probably register the highest values in the third quarter, with a tendency to delay in the winter months.

The most important factor for the accelerated total economic growth in terms of **demand**, which continued in the second quarter, is the accelerated growth in the export of goods and services with a share of 7.3 percentage points in GDP growth. At the same time, the share of domestic demand went up to 10.6 percentage points as a result of accelerated growth in investments against delayed growth in final consumption. Thus, imports accelerated and their negative share in GDP growth went up to 11.5 percentage points. Like in the first quarter, import of goods and services registered higher growth against exports. Consequently, the share of imports in GDP stood at 82.1 per cent – a new record-breaking value for the period since 1996, very close to the only higher value of 85 per cent registered in the first quarter of 1997.

The expected delayed growth in final consumption was registered as early as the second quarter. Growth in **investments** accelerated to 16.8 per cent, outpacing growth in the previous quarter, which stood at 9.2 per cent, and registering much higher values compared to the second quarter of last year. Growth factors include higher Government capital expenditures by 45.8 per cent against the first quarter.

In the first half of 2005, the share of investment in GDP went up to 25.5 per cent and the **financing of investment** is due mainly to the growth in foreign savings. At the same time, national savings decreased as a result of decline in domestic savings, whereas the share of net current transfers and net foreign income in national savings remained more or less unchanged.

In the third quarter, the national **business climate** remains favorable, but the dynamics of the Estat index of business climate and NSI's monthly business surveys indicates delay in the upward trend of total economic growth observed since the beginning of 2005. In July the value of the **ESTAT index** of business climate in Bulgaria went down to 3.12 compared to the April value of 3.55. Unlike the usual growth of optimistic expectations in the summer, the index value remained unchanged, registering actually a slight decline. The political dynamics after the end-of-June elections broke the outlined seasonal cycle of the business survey results. The long and difficult process of cabinet formation intensified the negative assessments about the environment and generated preventively more sceptic expectations in the business.

NSI's general business climate indicator registers decline for a third consecutive month, having reached in June a long-term maximum since 1994 (35.4 per cent). In July, it decreased by 3.5 percentage points, in August – by another 2.3 points and in September – by 3.4 points. The September level of the general business climate indicator is the lowest since the beginning of 2005.

In the period January – July 2005 the balance of payments **current account** deficit registered accelerated growth, again mostly because of the deteriorated balance of trade deficit along with the growing deficit in incomes and the decreasing positive balance in services and current transfers. About 20 per cent of the deteriorated trade deficit is a result of changes in the prices of energy resources. The balance in services is positive but decreases against the same period of last year, despite the positive balance in "Travel", because of the deteriorated balances in the "Transport" and "Other Services" components. Growth in proceeds from travel registers delay. Paid investment income accelerates compared to received income mostly because of the higher growth in paid direct investments. Proceeds from money transfers, which account for 75 per cent of total proceeds from transfers, register negligible increase against the first seven months of 2004. The foreign direct investments cover of the current account deficit deteriorates and will probably remain below 100 per cent for the current year.

Growth in **foreign trade** indicates that the economy functions quite well, and signals stable economic development. It results in significant trade deficit, yet with lower growth in the first half of 2005 against 2004 (28.9 and 38.7 per cent, accordingly). Unfortunately, this growth accelerated again in the third quarter. Higher imports (mainly machines and equipment, prime and raw materials) mostly result from higher investments (domestic and foreign). These investments and the import they generate form the basis of a future growth in exports. Bulgarian companies have already invested in renewal of facilities aimed at enhancing productivity, improving quality and satisfying the high market requirements, and their production is increasingly export-oriented.

The record-breaking economic growth in the second quarter of 2005 is accompanied by much slower growth in employment. The positive result is that for a second consecutive quarter **labor productivity,** measured as GVA per employed person, registers higher growth compared to employment.

In the beginning of the third quarter, **unemployment** decreased to 332.9 thousand people and the unemployment coefficient (based on a labor force survey method) went down to 10 per cent or 2 percentage points below the level for the same period of last year. However, the share of permanent unemployment went up from 57.4 per cent in mid 2004 to 60.4 per cent. The share of the unemployed looking for first employment increased as well, indicating lack of correspondence between labor demand and the training young people get in the Bulgarian education system. The Employment Agency registered for the first time decrease of registered unemployment to values below 400 thousand.

In the period July – October **the enterprise policy** was influenced by the post-election environment and was mainly focused on completing projects and measures initiated by the previous Government:

- Promoting and implementing projects for the support of entrepreneurship and SMEs;
- Facilitating the start up of new business by passing the BULSTAT Act;
- Completing public procurement notices on-line;
- Implementing measures for the introduction of European standards;
- Intensifying the activity of the Bulgarian Export Insurance Agency.

The new Government declared its intention to enhance **public-private partnerships** in the construction of Bulgaria's national infrastructure. It concentrated on the fight against corruption, which prevents the development of legal business in Bulgaria. According to CED, the priority problems, which the new Government should solve in order to improve the business environment, relate to:

- Overcoming the lack of confidence in the fairness and transparency of public procurement procedures;
- Facilitated procedures for the start up of new business;
- Proceeding with structural reforms, including privatization and concession of monopolies and of infrastructure;
- Cutting corruption practices.

Public finance development is characterized by persisting major trends from previous periods, including growth in budget surpluses and decreasing foreign debt. At the end of August, budget surplus reached BGN 1 318 m or up BGN 127 m on the end of August 2004 level and up BGN 589 on the surplus at the end of August 2003. From May till August, foreign debt decreased by EUR 584.3 m.

The tax legislation amendments proposed by the Ministry of Finance bring some certainty as to the tax policy of the new Government, and declared expenditure intentions give idea about Budget 2006 priorities. Most notable among the requests for increased expenditures is that of the minister of labor and social policy (an increase of some BGN 500 m), which is generally intended for increase of salaries and wages in the public sector and of pensions. Tax and social security amendments consist in reduced pension insurance contributions by 5-6 per cent, higher exemption limit of personal income tax from BGN 130 to BGN 180, increased excise on alcohol, cigarettes and fuels and increased tax assessment of property by 20 per cent. Proposed amendments actually transfer the tax and social security burden from direct to indirect taxes while the reduction of the total tax and social security burden is negligible.

According to CED, priority public finance development areas for Bulgaria include:

- Stopping the practice of growth in budget surpluses and switching to a balanced budget;
- Eliminating the opportunity for the Government to make expenditures in excess of budgeted funds;
- Limiting the budgetary distribution up to the planned 40 per cent and gradually decreasing this level by about 1 percentage point per year;
- Restructuring and improving the tax collection system, particularly making the National Revenues Agency (NRA) operational;
- Changing the philosophy of the substantive tax system towards less state intervention in the economic decisions of business entities;
- Steadfast introduction of fiscal decentralization;
- Reducing the total tax and social security burden on the basis of a sound economic concept;
- Introducing family income taxation.

Against the background of continuing decrease of unemployment, the intention of the coalition cabinet of BSP, NMSS and MRF to create 240 000 jobs and **to decrease registered unemployment** to levels below 10 per cent in four years seems acceptable and realistic. However, the issue of the quality of new jobs, which should not only decrease unemployment but also guarantee permanent employment, remains open.

In the next few years, the Government will have the hard task to solve labor market problems concerning high permanent unemployment and the lack of correspondence between labor market demand and supply in terms of education and qualification requirements. The labor market policy should help to overcome the big regional differences in employment and unemployment and to create employment for people of low education and for the permanently unemployed.

The upward trend in real **incomes** persisted in the first half of 2005. Growth in real incomes in 2004 and 2005 means improved prosperity and higher saving power.

The July 2005 consumer price survey registered more pessimistic expectations about the consumer price dynamics in the next 12 months. Assessments about the financial condition of households deteriorate and pessimism about the future increases. Such expectations follow from a more unstable general political and economic situation in the summer and from the increase of fuel and energy prices.

The minister of labor and social policy declared the **"active income policy"** a priority of her term of office. However, the Ministry of Labor and Social Policy has not yet come out with details of the goals and instruments of this policy. Such a position is explainable by BSP's election pledges for a single increase of public sector salaries and wages by 20 per cent. The inertia of past years, when the State was the biggest employer and Bulgaria was going through a series of inflationary processes, also has its effect. This type of income policy should be left in the past. In 2005, when the Bulgarian economy is predominantly private and develops in an environment of price and financial stability, such policy is neither needed nor possible.

Issues like increase of public sector salaries and wages and of the minimum wage, Christmas allowances to salaries and pensions, which were highly debated in recent months, should be dealt with very carefully, taking strict account of budget resources, giving proper weigh to the higher labor productivity, and preserving financial stability.

According to CED, major social policy priorities should include:

- Improved quality of new jobs which should guarantee permanent employment and professional qualification to the unemployed;
- Reorientation towards permanent employment at the expense of community activities under subsidized employment programs;
- Achieving correspondence between labor market supply and demand through targeted education and training policy and education reforms;
- Shifting from a social policy of indiscriminate money giving to income policy based on economic efficiency.

In the **pension insurance** field, Bulgaria has witnessed for the first time political will to lower the social security burden, which is assessed positively by the business and the syndicates, as well as by the expert community. To ensure long-term financial stability of the pension system, the Government should:

- Support the set up of a so-called "silver fund";
- Implement the necessary legislative measures to make the National Revenues Agency operational;
- Take further steps to improve the mechanism of syndicate-employer negotiations on the annual minimum social security thresholds which will go up by an average of 8 per cent in 2006.

The new leadership of the Ministry of **Health** seems willing and ready to continue the reform in the health sector, but first there is a need of a publicly coordinated political vision about the Bulgarian health model development. Important health sector challenges, which the new coalition cabinet should address with adequate measures in place, concern the need to:

- Change the financing mechanism for hospital care institutions towards personal participation by patients;
- Limit the basic package of NHIF-financed services;
- Take efficient measures to develop private health insurance funds;
- Carry out efficient privatization of medical institutions;
- Build an integrated information system in the sector;
- Solve the problem with uninsured persons, and
- Ensure transparency of tenders for medicines.

The latest **environmental** legislation amendments are a prompt response to European Commission's critical assessment about the fulfillment of commitments under Chapter "Environment". However, government administration actions are still at the level of policies and measures and come down to formulating administrative impact approaches.

For the business and the consumers, the generous pledges for improved quality of life and healthy living conditions in the parties' election programs come down to the ability of the State to create optimal administrative environment where economic incentives, voluntary actions and corporate social and environmental responsibility will not seem only exotic wishes.

The banking system still dominates the financial sector and financial intermediation. The last quarter statistics clearly show that, as we expected, credit expansion was subdued only temporarily: calming down in May and June, in July and August it reached again its former levels of 45 per cent on an annual basis, which again brings to the front the risk for the Bulgarian banking system stability in a long-term perspective. Growth in money supply for the last 12 months continues at threatening levels of 28.3 per cent. Confidence in the lev persists; the share of the deposits with commercial banks in BGN increases. We insist again that BGN should abandon the administrative approach in their attempt to subdue credit expansion and should adopt market-oriented measures.

In the **energy sector,** the oil "tsunami" coming from the international markets swept over Bulgaria as well. The prices of all oil-bound energy resources went up. Expected increase effects include higher inflation and delayed economic growth. The State plans to restructure the large transfer companies Bulgargas and NEC before their privatization. The Government does not exclude the possibility to renegotiate with the EU the time limits for restructuring of the two companies. The new Government will continue the construction of Belene NPP, while it will probably stop the vertical and horizontal division of the energy companies. The Cabinet believes that it can find another restructuring model, which will guarantee a competitive Bulgarian energy sector in the single European market.

According to CED, priorities for energy sector development include:

- The State should minimize the barriers to free trade in the sector;
- Accelerate the competition procedures for concession of the other gas-distribution regions;
- Find the optimal combination of responsibility, risk and yield for the State and for the possible private partners in the construction of Belene NPP;
- Ensure timely implementation of the rehabilitation projects for and privatization of the big TPPs.

Floods were the top event in the **transport sector.** They incurred huge damages to the railway transport and to new Government's declared priorities. The Ministry of Transport outlined five priorities for the future management:

- Transport system safety and security;
- Transport system modernization;
- Accelerating projects financed from the pre-accession funds;
- Improving the quality of transport services – developing a national transport scheme binding the different transport sectors;
- Enhancing the dialogue with the business.

According to CED, important transport sector tasks include:

- Coordinated and efficient transport policy;
- Accelerated sector privatization using only competition-generating market mechanisms;
- Transparency and publicity of all processes in the transport sector.

In the third quarter of 2005, **tourism** development continued at a high pace with number of tourists going up 4 per cent on the same period of last year, but expectations about permanent boom were not fully justified. Optimistic anticipations were underpinned by huge investments in special infrastructure and by the doubled number of beds in some resorts. The opportunities of special forms of tourism like rural, eco, cultural, game, congress, spa and other, remain underutilized. Typical problems for Bulgarian tourism like **excessive construction;** shortage of qualified labor; poor road, water-supply, and sewerage infrastructure; country's lack of popularity as tourist destination, emerged again in the summer season.

The new Government has outlined two priorities of the state policy for tourism – encouraging local and regional initiative and promoting public-private partnerships. That will enable decentralization through cooperation of the State, the local government, the branch organizations and the private sector. The objective is to intensify regional development and to create new jobs on municipal level. In the new Government structure, tourism will be taken out of the Ministry of Culture. The sector will be managed by a Tourism Agency and the Ministry of Economy and Energy will be the spending unit of budgetary funds. According to CED, the basic tasks in this field include:

- Developing a National Tourism Development Strategy;
- Passing the Black Sea Coast Act which could curb excessive construction in the big resorts;
- Targeted solving of infrastructure problems in major tourist centers;
- Solving the problems of the current year shortage and deteriorating quality of labor in tourism;
- Intensifying the marketing and advertising of Bulgaria as a tourist destination.

The heavy summer rains damaged the crop in many **agricultural** regions. They hit most the production of fruit and vegetables, vines and perennial plants. Overall, damages will not have significant effect on the market, but they will create problems to the processing enterprises. The data from the completed census of farms provides a clear picture of the real situation in the sector. Land fragmentation and the small size of farms are major sector characteristics. Only in the grain sub-sector, production is concentrated in larger companies and tenants, as well as in well-functioning cooperatives, which can achieve higher productivity. In the other sectors, there is a need of urgent farm consolidation and set up of functioning producer's organizations with a view to utilize the money from European funds. The new MAF management declared the set up of Paying and Intervention Agency (based on State Fund Agriculture) and an Integrated Administration and Control System to manage the money from European funds after 2007 its basic priority. Financing from State Fund Agriculture is also intensified; higher attention is paid to farmers training and to the provision of information, consultations and technological assistance. Development of land relations and consolidation are also among ministry's declared priorities. The objective is to accelerate the preparation for Bulgaria's accession to the EU, gradually redirecting efforts from national to regional and farm level. According to CED, special focus should be placed on:

- Mobilizing efforts to successfully complete the SAPARD Program until it is terminated upon Bulgaria's accession to the EU;
- Creating the necessary institutional infrastructure, organization and capacity to manage the money from the structural funds after 2007.

Major **regional policy** events include approval of measures by the Council for European Integration for Bulgaria's preparation to manage the structural funds, and presentation of draft regional development plans (at planning region level). According to CED, the necessary steps in this field include:

- Accelerated process of drafting planning and strategic documents to manage the money from EU's cohesion and structural funds;
- Implementing proactive policy to inform the business and the people about the challenges and opportunities of accession and of structural funds;
- Taking steps to enhance the institutional capacity of the central and local administrations to manage the money from European funds.

The third quarter of 2005 did not bring significant changes to the **high technology and communications** sector. The 2004 growth in the volume of the Bulgarian telecommunications market went up 13 per cent on the previous year, accounting for about 7 per cent of total GDP and registering again higher values compared to GDP growth. The new Government declared priorities, which more or less continue in the path of the pervious cabinet. The tenders organized for individual „point-to-multipoint" licenses are the most important event, which will have serious effect on future sector development.

In the first months after their constitution, the new Bulgarian legislative and executive bodies passed and issued a limited number of **laws and regulations** governing economic relations and the business environment. Amendments and supplements to the Commercial Code were passed with a view to align Bulgarian company law with the European directives. The first group of amendments is in the general section of CC and covers trade law **publicity, validity of the actions** of company's bodies with respect to third persons, and the **invalidity** of companies. The second group of amendments and supplements concerns the change **of the capital** of joint-stock companies with a view to protect and guarantee the interests of shareholders and of third persons, and the third group concerns **the registration of branches of foreign commercial companies** on the territory of the Republic of Bulgaria. The amendments introduce new rules concerning the regulations for transformation of commercial companies with a view to facilitate these procedures for sole-proprietor commercial companies.

Amended and supplemented was also the subject matter of public offering of securities, technical requirements to products and public procurement.

Insurance Code is pending approval. It will repeal the Insurance Act and will introduce significant amendments in the insurance field, in line with EU directives.

Gross Domestic Product

Economic growth. Preliminary NSI estimates[1] confirmed our supposition that in the second quarter the conditions are in place for growth on an annual basis to exceed growth in the first quarter. Real growth[2] in economy for the second quarter is estimated at 6.4 per cent as compared to the second quarter of 2004 when growth was measured at 5.5 per cent[3]. This is the highest economic growth figure for a given quarter ever registered over the past seven years.

The highest contribution to growth in the economy in the second quarter belongs to services on the supply side and exports on the demand side; the most dynamic items being industry and investment, respectively.

In spite of the fact that the overall business environment in the country remains favourable during the third quarter, monthly NSI business surveys reveal signs of a slow-down in the upward trend of overall economic growth observed from the beginning of this year. We expect that overall economic growth will continue to be high but will experience a slow-down (at levels of 5.6 – 5.8 per cent for Q3; nevertheless our expectations for the entire 2005 are in the range of 5.7 – 5.9 per cent, i.e. higher growth as compared to the 5.6 per cent reported for 2004[4].

Supply. In the second quarter of 2005, GDP growth on the supply side was triggered by the growth in value added for the economy as a whole by 6.2 per cent and growth in adjustments[5] by 7.7 per cent. The renewed growth of the Adjustments item is possibly due to the declining growth rate of financial intermediation and the upward trend in the import of goods rate as compared to Q1 rates. As a result, the increase of the Financial Intermediation Services Indirectly Measured (FISIM) is lower as compared to the increase in the component "Net Taxes (excise duty, duty tax, VAT, less subsidies) on products". This is further confirmed by certain decline in the otherwise high growth rate of value added in financial intermediation (from 32.3 per cent in the first quarter to 30 per cent in the second quarter) and the speedier growth in the import of goods and services (to 15.5 per cent which is higher both as compared to 10.8 per cent growth for the previous quarter, and as compared to the 11.1 per cent growth for Q2'2004).

Growth by Economic Sector. Growth in both industry and services is gaining speed as compared to the second quarter of last year. The growth rate in industry continues to accelerate as compared to the previous quarter while growth rate in services is slowing down. Thus industry is now ahead of services by 2.9 points over 0.8 per cent points in the first quarter. Decline in agriculture is deepening even further.

In spite of its certain decline by 3.4 percentage points (from 3.9 percentage points in the first quarter) the services contribution to the Gross Domestic Product growth is still highest. Value added for services grows by 6.4 per cent (at 7.4 per cent for the previous quarter and 5.7 per cent for Q2'2004). Finance (at 30 per cent growth) and trade (14.3 per cent) continue as leading branches in the dynamics of services.

Industry is still the fastest developing sector (9.3 per cent growth in value added). Boasting accelerated growth (11.5 per cent, following the 9.7 per cent in Q1), processing industry contributes 2 percentage points to GDP growth. Notwithstanding a certain slow-down as compared to the previous quarter, growth in construction is still highest (13.8 per cent, following 14.2 per cent for Q1'2005) .

The dynamics of short-term indicators in industry[6] over the past months shows signs of certain balanced reaching of potential for accelerated growth in industrial production, for example the Business Climate in Industry indicator is hovering around its average levels for the past twelve months; starting in June, export sales are growing at a slower rate compared to domestic sales. This shows that growth in industry might continue high, but will hardly continue to accelerate. In construction, we'll probably witnesses the highest point in growth on an annual basis in Q3, with a trend of slowing-down in winter months.

The decline in value added for the agricultural sector persists and is now over the 5 per cent mark (following minus 1.7 per cent for the previous quarter and minus 0.4 per cent for Q2'2004).

Growth by type of ownership. Added value in the private sector is up by 9.1 per cent, and down by 3.4 per cent in the public sector over the second quarter of 2004. At the same time labour force survey data show that the number of persons employed in the private sector is growing on an annual basis by 4.4 per cent while it declines by 5.5 per cent in the public sector. In the private sector, the positive trend of leading growth in productivity continues (measured as value-added per one

1 Source: NSI, national accounts data, published 19 September 2005 AEAF, Recent Development Analysis.

2 All data on GDP growth and its components are related to the real growth on an annual basis, i.e. related to the relative change in volumes over the review period as compared to the volumes for the respective period of the the preceding year when applying constant prices.

3 It should be reminded that the first growth estimate for the second quarter of 2004 was 6.0 per cent, revised at 5.5 per cent with the publication on 31 March 2005 of the revised GDP data for 2003 and for the first, second, and third quarter of 2004, and estimates for the fourth quarter of 2004 and for the entire year 2004. The revision of national accounts data is a necessary and imminent procedure when receiving additional and more complete statistical information of the monitored indicators.

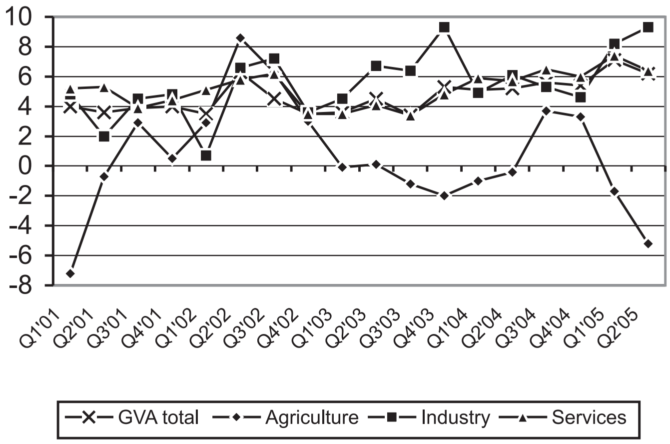
4 AEAF (The Bulgarian Economy: Analysis and Outlook, July 2005) forecast a 5.3 per cent GDP growth for Q3 and 5.2 per cent for the year; the same forecast for the year was also quoted in the paper entitled "Main Macroeconomic Indicators Forecast for Bulgaria 2006-2008" of 29 August 2005. The BNB projections (Economic Review, August 2005) are in the range of 5.4 – 5.8 per cent for the year.

5 When calculating GDP using the production method, the following methodological link is used: Gross Domestic Product (market prices) = Gross Value Added (basic prices) + Adjustments, Adjustments being = Net Tax (excise duty, duty tax, VAT, less subsidies) divided by products **less** Financial Intermediation Services Indirectly Measured (FISIM). The Financial Intermediation Services Indirectly Measured component is included under "Adjustments" with a minus sign as it represents the financial intermediaries' products which is assumed to be entirely used for intermediary consumption; however as it is not possible to spread it statistically to individual producers, the adjustment is calculated at national level.

6 Source: NSI (Business ConjunctureMonthly Business Surveys; Sales and Production Index in Industry), AEAF, Recent Developments.

person employed) as compared to the growth rate in the number of persons employed.

Figure 1. Added Value by economic sectors, real growth over the respective quarter of the preceding year, %



Source: NSI

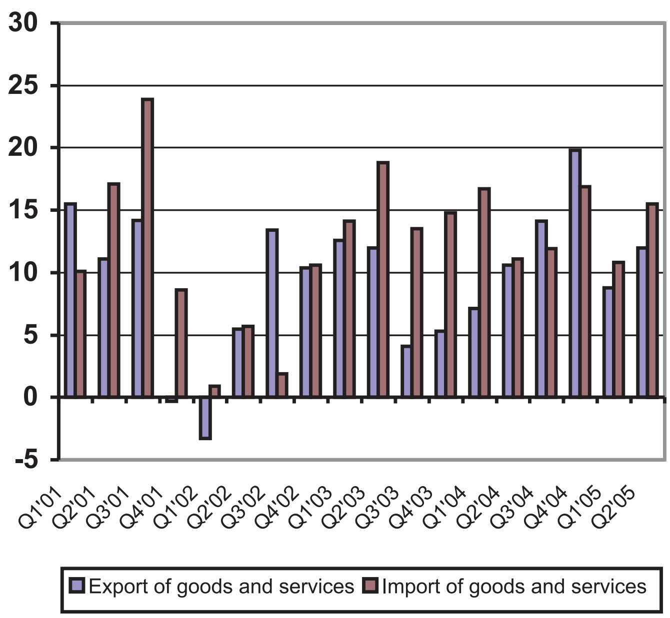
Demand. Of greatest importance to the continued momentum in overall economic growth in the second quarter of 2005 is the accelerated growth rate in the export of goods and services reaching a 7.3 percentage points contribution in GDP growth rate. Meanwhile the contribution of domestic demand grew to 10.6 percentage points, accounted for by the speedier growth in investment in an environment of slower growth in final consumption. This resulted in such accelerated growth in import that its negative contribution to GDP growth climbed to 11.5 percentage points and the total negative contribution of external trade in goods and services deteriorated reaching 4.2 percentage points (at minus 1.7 percentage points for Q2'2004 and following minus 2.5 percentage points for Q1'2005).

Consumption. The slow-down in final consumption growth we predicted emerged as early as the second quarter (5.9 per cent growth on an annual basis, following 7.3 per cent growth for the first quarter). In spite of the fact that individual consumption growth (5.7 per cent) still exceeds the average income growth per household member (5.4 per cent)[7], the difference is shrinking; in the first quarter the difference was determined respectively by 7.3 and 5.8 per cent on an annual basis and was mostly due to the lending peak in that period. Thus the share of individual consumption in GDP shrank from the record-high 83.7 per cent to 79.3 per cent. The relatively high growth rate of collective consumption is still above 7 per cent; thus its share in the quarterly GDP continues to be quite high for a second successive three-month period, being above the 10 per cent mark.

Investments[8]. Growth in investment accelerated to 16.8 per cent, considerably higher as compared to the growth rate in the previous quarter (9.2 per cent) and even higher as compared to Q2 of last year (6.9). According to AEAF one of the factors that contributed to the higher rate of investment in the second quarter of the year, was the increase by 45.8 per cent in government capital expenditures over the first quarter.

Export/Import of goods and services. The export of goods and services grew in the second quarter by 12 per cent (following 8.8 per cent for the preceding quarter and 10.6 for the same period of last year). As was the case in Q1, the imports of goods and services grew faster than the exports. Growth in imports by 15.5 per cent (following 10.8 per cent for the preceding quarter and 11.1 for Q2'2004) resulted in an 82.1 per cent share of imports in GDP – a new record-high share since 1996, very close to the next highest: 85 per cent in the first quarter of 1997.

Figure 2: Exports and imports of goods and services, real growth over the respective quarter of the preceding year, %



Source: NSI

Financing of investments. The increased share of capital formation (25.5 per cent of GDP, at 23.6 per cent for the first half of last year) is due to the increase in external savings (reaching 15 per cent percent of GDP, at 11.2 per cent for the six months of 2004) in an environment of shrinking national savings (to 10.5 per cent percent of GDP over 11.9 per cent for the six months of 2004). National saving goes down due to the decreasing domestic savings rate while the share of net current transfers and net foreign income in national savings for the half-year remains relatively constant as compared to the first half of last year. (Table 1).

7 Household budgets statistics and own estimates.

8 For the sake of shortness, we are using the term *Investments* instead of the *Gross Fixed Capital Formation,* which consists of acquisitions of tangible and intangible long-term non-financial assets, including adjustments for work-in-progress. Source: NSI.

Table 1. Financing of gross capital formation

	Financing, total	Gross national savings, total	Gross domestic savings	Current transfers from abroad, net	Income from abroad, net	Foreign savings
In % of GDP for period						
six months '2005	25.5	10.5	8.5	4.4	-2.3	15.0
six months '2004	23.1	11.9	10.1	4.1	-2.2	11.2
six months '2003	20.3	7.6	9.3	3.3	-5.0	12.7
six months '2002	19.1	12.6	11.1	3.3	-1.8	6.5
six months '2001	17.7	11.5	9.6	4.1	-2.1	6.2
Total financing =100, %						
six months '2005	100	41.2	33.2	17.1	-9.2	58.8
six months '2004	100	51.6	43.5	17.8	-9.6	48.4
six months '2003	100	37.4	45.9	16.2	-24.8	62.6
six months '2002	100	66.1	58.0	17.3	-9.2	33.9
six months '2001	100	64.9	53.8	23.0	-9.2	35.1

Source: BNB, Balance of payments, published, as of 12 September 2005; NSI, GDP, published as of 19 September 2005 and own estimates

Current Account.

The current account deficit accumulated from the beginning of 2005 until July[9] is growing at an increased pace; traditionally the biggest negative contribution to this is the deteriorated negative trade balance alongside the increase of income deficit and the lower positive balance on services and current transfers. The current account deficit reached 7 per cent of the annual GDP[10] (at 3.9 per cent for the same period of last year and 7.5 per cent for the entire 2004). At this rate and the emerging GDP figures for 2005, the total current account deficit for the year is expected at 9.5 per cent percent of GDP.

The trade deficit (FOB) grew at 9.5 per cent percent of GDP (for the seven months of last year it ran at 7.4 per cent of annual GDP). The deterioration of trade deficit of about 20 per cent by EUR 575 m as compared to the same period of the preceding year is due to the changed prices of fuels.

Export (FOB) and import (FOB) in nominal terms have grown as compared to January-July 2004 by 19.0 and 24.2 per cent, respectively. After adjusting for the higher prices of crude oil, petrol products and natural gas, the increase in imports and exports are recalculated at 16.5 per cent and 20.4 per cent, respectively.

The negative balance between the import of crude oil, petrol products and natural gas and the export of petrol products grew to 3.3 per cent percent of GDP, at 2.5 per cent for the seven months of last year.

The balance for services for the seven months since the beginning of the year is positive, but going down as compared to the same period of last year. In spite of the increase of the positive balance on the Travels item, because of deteriorated balances for the component positions of "Transport" and "Other Services".

When set against the annual GDP, the services balance is down to 1.6 per cent percent of GDP, at 2.3 per cent for the same period of 2004. The positive balance under the Travels item grew respectively from 2.9 to 3.0 per cent percent of GDP, the negative balance on transport services went up from 0.7 to 0.9 per cent percent of GDP, and the Other Services balance was negative accounting for 0.5 per cent percent of GDP, unlike last year when it was only 0.1 per cent but preceded by a plus sign. It should be noted that in spite of the increase in proceeds from traveling in Euro by 10.2 per over the same period of 2004, the growth rate is slowing down as compared to the growth rates for the same periods of 2002-2004: thus in 2003 the increase in revenues from travels was 19 per cent and in 2004 revenues grew by 23 per cent over the seven months of the preceding year.

The negative balance under the "Income" item is growing (reaching 1.4 per cent percent of GDP, at 1.3 per cent for the seven months of last year) due to the higher growth rate of payments on investment income as compared to income received. Income paid is on the rise mostly due to the growth in payments on direct investment (55 per cent), of which payments of dividends are 2.3 times more as compared to the seven months of 2004. Payments on "Other Investments" are also up significantly – by 42 per cent.

Although net incoming current transfers in absolute terms are slightly on the rise, their share in GDP is down to 2.3 per cent from 2.4 per cent for the seven months of 2004. Proceeds from cash transfers which represent 75 per cent of the total volume of transfer proceeds are only registering a slight increase as compared to the seven months of last year (0.7 per cent).

The coverage of the current account deficit with foreign direct investments is deteriorating, reaching 56.2 (for the same period of last year it was 130.4 per cent). This ratio is lower even than

9 Source: BNB, Balance of Payments, published, as of 12 September 2005

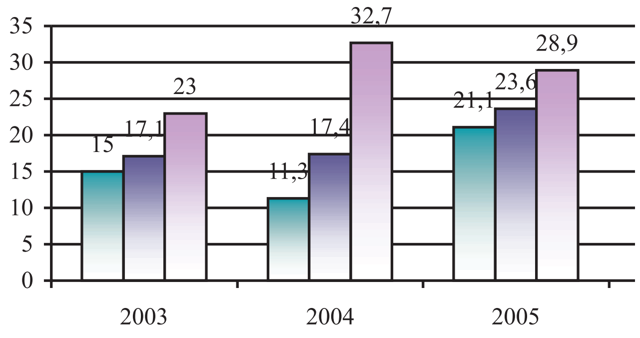
10 GDP for 2004 – EUR 19,433.7 m (NSI estimates) and projected GDP for 2005 – EUR 21,177 m.

the ratio for the entire previous year (146.1 per cent) and will probably stay below 100 per cent for the entire current year.

External trade

An indicator of the relatively good state of economic functions and development is the *growth rate in increase in trade* in nominal terms (23.2 per cent during the second quarter and 22.6 per cent for the first half-year in nominal terms). This was achieved in an environment of weak growth within the EU (a major market for Bulgarian products), growing oil prices (and, consequently, of production costs) and the Bulgarian Lev in a strong position to USD. The growth rate in imports (23.6 per cent for the first half of 2005 over the same period of the preceding year) is still ahead of growth in exports (21.1 per cent) but the difference is considerably smaller than one year earlier when these rates were 17.4 and 11.3 per cent respectively. We could expect this trend of leading growth in imports to continue for at least one more year on the background of the process of recapitalisation of the economy and its preparation for the European market. This means that the trade balance deficit (exports FOB – imports CIF) will continue to rise although at a slower pace (28.9 per cent for the first half of 2005 as set against 38.7 per cent for the previous year).

Figure 3. Growth rate in nominal terms of exports, imports and the trade balance deficit during the first half of the year over the same period of the preceding year, %



Imports growth (mostly of machinery and equipment and raw materials and supplies) is based on the increase in investment (local and foreign). At the same time however these investments and the import they bring about are in themselves a precondition for future growth in exports. The other factor contributing to the increase in imports - the sharp upward curve of oil prices on the international market, had an adverse impact on exports as it results in an increase in production costs, loss of market positions and shrinking investment. All of the above results in an increase in the trade balance deficit.

The volume of exports for the 8 months of the year amounts to EUR 6, 020 m - the largest ever achieved so far. Imports went even higher – EUR 8, 420.8 m., forming a deficit of EUR 2, 400.8 m for the period. On the background of growing international prices, the value of imports and exports will continue to grow even faster the increase of physical volume.

The product structure of exports shows insignificant changes. Raw materials continue to be the major share of export (about 45 per cent) due to the favourable international market settings. Strong demand and high prices of metal, some chemical products and plastics, raw materials for food manufacturing and textile results in increase in the export of these items by more than 26 per cent on an annual basis. In the second place, following raw materials, are consumer goods, but their share continues to go down. The major subgroup here (accounting for 55 per cent of all consumer goods) are clothing and shoes. The volume in terms of value of exported product in this subgroup registers a slight decline and its share in total exports is going down. This was an expected consequence following the revocation of Chinese textile quotas and the strong competition on the European market. The decline in the volume of textile and clothing exports however was considerably lower than expected and it now seems that Bulgarian producers will keep their positions as suppliers of clothes. The highest increase is seen in investment goods (36 per cent during the first half of the year) which lead to an increase in their relative share to 16-17 per cent of total exports.

The geographical structure of exports remains unchanged: almost 60 per cent of Bulgarian products are sold in the EU market. Maintaining such a large share in total exports for this strongly competitive and highly demanding market is a good testimonial to the competitiveness of national production and the economy's ability to cope with competitive pressure. Ranking second, with 21 per cent of exports, is export to Balkan countries. Almost half of the products exported to these is placed on the Turkish market; exports to Turkey registered an almost two-fold increase within the space of two years. With the gradual recuperation of the economies of countries in the so-called Western Balkans and the establishment of bilateral free trade areas, exports for the region are registering a visible increase.

Product structure of imports. The largest share in the increase of imports is that of energy resources and investment goods. Only during the second quarter of 2005, the imports of investment goods grew by 31.7 per cent over the same period of the preceding year. Thus, its share now reached 27.7 per cent of total imports. The largest increase is registered for vehicles and spare parts. Because of the high prices of oil, the share of imported energy resources during the second quarter grew to over 18 per cent, at 16.8 per cent for the respective period of 2004, and 17.5 per cent for 2003. The smaller growth in consumer goods import is seen as a positive trend when compared to the general rate of increase and decrease of the share of these goods in total imports. The largest share is now registered by automobiles and food products in connection with the growing consumer demand on the domestic market. The change in the imports of various raw materials clearly shows the connection with export trends: the supply of ferrous and non-ferrous ores and concentrates is growing, and textile materials mostly remain unchanged.

Geographical structure of imports. Traditionally, Bulgaria's major partner is the European Union with over 50 per cent of imports. Improved regional contacts lead to the increased significance of Balkan countries for providing basic raw materials and supplies. Their share exceeds 11 per cent and imports from Romania and Turkey register an increase of 50 per cent on an annual basis.

Forecast. We have all reasons to expect that exports will continue to grow steadily (by about 20 per cent) because the majority of existing enterprises have already invested in renewing their plant capacity to improve productivity and quality and meet the demanding market requirements. Many of the newly established enterprises with foreign investment also started producing not only for the domestic market but also for exports. Thus the improved competitiveness of the economy due to greenfield investment will provide for the stable growth in exports; the only risk now seems to arise from apprehensions on the shrinking consumer demand in the Euro-Zone. In the near future the prices of crude oil and raw materials as a whole will impact significantly the increase in import and it will persist over 20 per cent. The growth rate in the machinery and equipment import will be associated rather with fresh investment and building new production capacity than with the renewal and certification of existing enterprises. We still believe that the increased trade deficit poses no risk to the economy because it is largely related to "catching up" of deferred investment consumption, a rising economic activity and accelerated integration of the national economy into the global economy while it is still financed by the inflow of foreign investment.

Foreign direct investments

According to a number of international studies, Bulgaria boasts the highest gross growth rate of foreign investment in the entire region, and occupies 12-th position in the world according to the level of foreign investment. For 2004, the country won greenfield investment projects representing over 2 per cent market share in Europe. Some of the factors behind this development are the economic and political stability; the mature economy; the presence of vacant market niches; the well qualified labour force; the presence of reliable local suppliers. Preliminary estimates show EUR 832 m in fresh foreign investment for the 7 months of the year or a decrease by about 15 per cent over the same period of the preceding year. These figures are rather incomplete and subject to numerous revisions. Although there are no major privatization deals during the period, by all accounts investors' interest to establishing and developing their business in the country remains very high. So the inflow of investment currently registered is the result mostly of greenfield investments and the expansion of existing production.

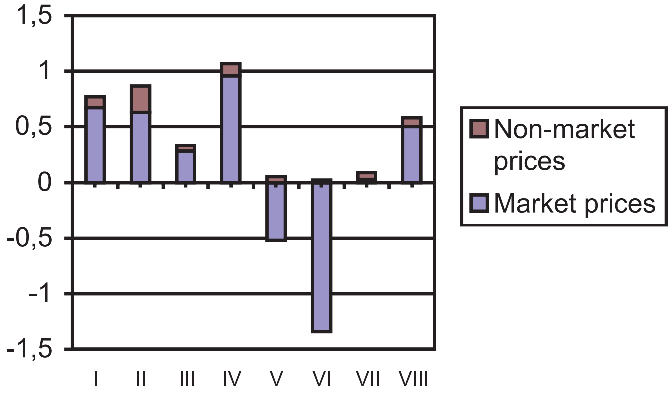
Expectations are that foreign direct investment will reach at least its last year's volume: EUR about 2 billion by our estimates (mostly at the expense of business-to-business and company internal loans and increase in capital). This forecast is based on the country's forthcoming EU membership, the stable macro-economic environment and the high economic growth. Additionally a large group of foreign investors are currently implementing investment projects for the modernisation of production processes, plant renovation, establishing better working conditions, achieving environmental compliance and further corporate development of companies.

Inflation

Consumer prices. In spite of the fact that, with two consecutive months of deflation (May and June), the total aggregated increase in consumer prices for the eight months since beginning of the year went down to 1.9 per cent, in August they were 5 per cent higher than August 2004. On average for the period, the increase on an annual basis is 4.4 per cent.

The monthly variation in consumer prices from January to August 2005 is mostly due to the market price dynamics on consumer goods and services and to a much smaller degree due to changes in administrative prices (Figure 4).

Figure 4. Contribution of market and non-market inflation in total inflation, percentage points



Source: NSI, AEAF

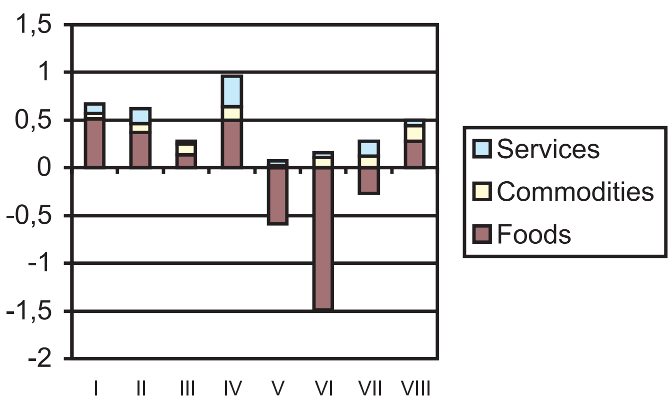
On its part, the overall dynamics of market consumer prices is defined mostly by the change in food prices (Figure 5).

The results of an econometric study[11] of the impact of annual price fluctuations of crude oil and the exchange rate course on consumer prices indices based on monthly data for the period

11 Source: BNB, Economic Review, August 2005.

2001-2004 reveal that 50 per cent increase in international fuel prices correspond to 0.33 percentage points contribution to inflation. . This effect is demonstrated mostly through the change in fuel prices: a 30 per cent increase in wholesale prices corresponds to 9 per cent increase in retail fuel prices which results in 0.3 percentage points in total consumer price inflation. The secondary effect on consumer prices which passes through the prices of transport services is seen as being very weak. A 30 per cent increase in wholesale fuel prices corresponds to as few as 0.03 percentage points contribution to inflation from the secondary effect.

Figure 5. Contribution of price change by groups of goods and services to market inflation, percentage points



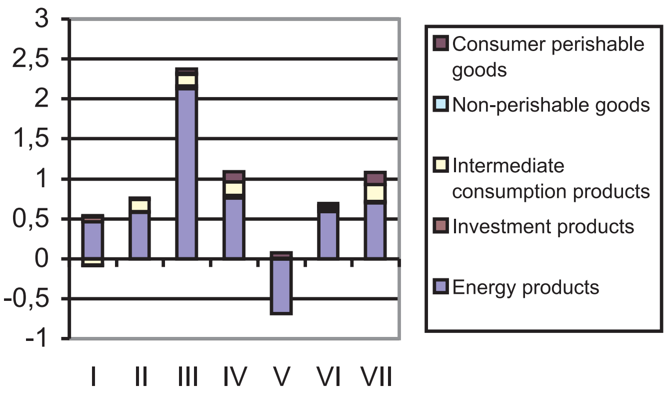
Source: NSI, AEAF

Producer price

Fluctuations in producer prices in industry for the domestic market are mostly influenced by fluctuations in the prices of the energy products group. Apart from being the group that is most strongly affected by price increases, this is also the group with the highest contribution to the total increase in producer prices (Figure 6). The BNB econometrical study quoted above shows that changes in international oil prices by 50 per cent are associated with a 30 per cent increase in the prices of the oil-processing industry and with a 3.54 percentage points contribution to the overall producer prices index in industry. The secondary impact of international oil prices on remaining industrial products is negligible and is estimated at 0.04 percentage points of the increase of the producer prices index in industry.

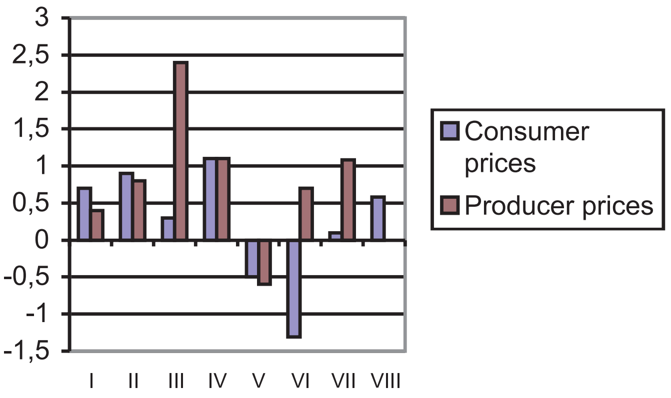
It is typical of an economy operating in an environment of steady economic growth for producer prices to have a wider range of monthly fluctuation as compared to consumer prices dynamics (Figure 7).

Figure 6. Contribution to producer prices fluctuation over the previous month by groups of products, percentage points



Source: NSI, AEAF

Figure 7. Change in consumer prices and producer prices in industry on the domestic market, previous month = 100 (%)



Source: NSI, AEAF

Unlike the prevailingly weak inflation expectations during the second quarter, in the three months of the third quarter NSI business surveys registered the prevailing presence of inflation expectations (Table 2).

Table 2. Expectations in the respective month of 2005 for an increase in the selling prices in the course of the next three months

	I	II	III	IV	V	VI	VII	VIII	IX
Industry	yes	no	yes	no	no	no	yes	yes	yes
Construction	no	yes	yes	yes	yes	yes	yes	no	yes
Retail trade	no	yes	yes	no	no	no	yes	yes	yes
Services (retail trade excluded)	no	no	yes	yes	yes	no	yes	no	no

Source: NSI, Business Conjuncture Monthly Business Surveys in 2005 and own conclusions

Employment, productivity and unemployment

The record-high economic growth for the second quarter of 2005 (6.4 per cent, at 5.5 per cent for Q2'2004) is accompanied by the considerably slower increase in the number of persons employed (1.3 per cent, at 3.3 per cent for Q2'2004) and the much faster decrease in the number of unemployed (by 18 per cent, 11.2 per cent for Q2'2004.)[12]. A positive outcome is that productivity continues to rise faster than employment.

Employment. On an annual basis, the number of economically active population continues to dwindle[13]. In the second quarter, the economically active population consisted of 3341.8 thousand people, which means 34.2 thousand less as compared to Q2'2004; those employed have increased by 39.1 thousand and those unemployed have decreased by 73.2 thousand.

The number of economically inactive individuals has grown by 30.2 thousand. In the second quarter these are 3333 thousand. (49.9 per cent of the population over 15) and of them, 1981.5 thousand fall within the 15-64 age group. The number of discouraged individuals goes down by 43.8 thousand, reaching 324.3 thousand, also declining is their share in the number of economically inactive people: from 11.1 per cent in the second quarter of last year to 9.7 per cent today.

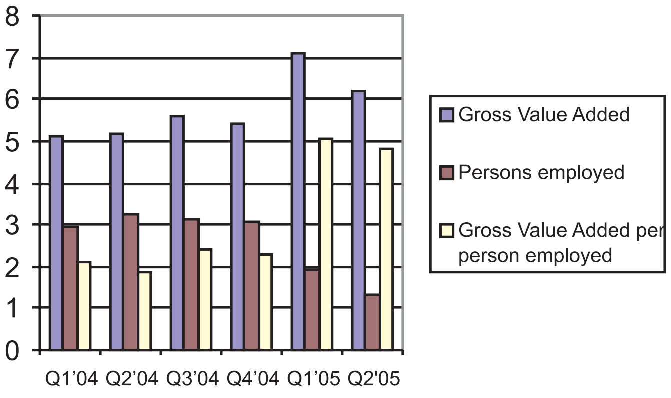
Those employed in the private sector account for 70.9 per cent of all persons employed (68.8 per cent in the second quarter of last year), their number has increased by 90.5 thousand people. Within the space of one year there have been changes towards keeping the share of employers (5.5 per cent), an increase in the share of people employed (from 77 to 80.1 per cent) and a decline in the share of self-employed (from 14.3 to 12.4 per cent) and the share of unpaid family workers (from 3.1 to 2.1 per cent).

Productivity. In the second quarter of 2005 productivity (gross value added per person employed) grew faster than employment (Figure 8). Unlike last year when the leading factor was increase in employment (estimated according to the available quarterly data from labour force surveys since 2003), in the first quarter of 2005 growth in labour productivity came ahead of the employment growth rate. If this leading growth in productivity is preserved, this would be a good sign for the process of intensification of the overall economic growth.

Unemployment rate.

The number of unemployed continues to go down, estimated at 332.9 thousand in the second quarter (or by 73.2 thousand less than the respective period of last year). As a result the unemployment rate (labour force survey methodology) fell to 10 per cent, or two percentage points below the level for the second quarter of last year.

Figure 8. GVA, persons employed, and GVA per person employed, total for economy – growth over the respective period of the preceding year (%)



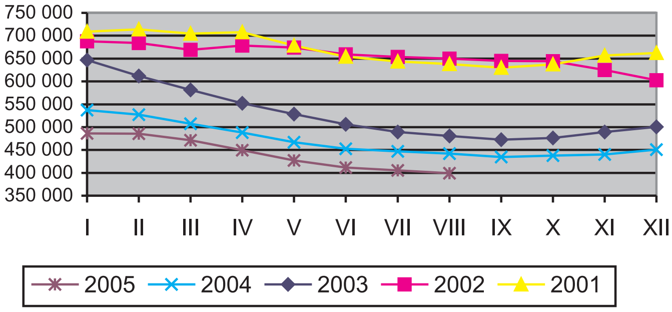
Source: NSI and own estimates

The number of long-term unemployed (1 or more years) was decreased to 201.2 thousand, or by 31.8 thousand. However the share of long-term unemployed people increased in the total number of unemployed (from 57.4 to 60.4 per cent).

Change in the structure of unemployed people as regards "previously employed/first job seekers" (from 79.4/20.6 per cent in the second quarter of last year to 76.8/23.2 per cent now) shows a certain shift in favour of people who had previous employment which works against first job seekers; this could mean a deteriorating structural misbalance between labour demand and supply at the expense of people entering the labour market.

As concerns the dynamics of registered unemployment according to figures supplied by the Employment Agency, August was the first month to register the number of unemployed below 400 thousand (Figure 9).

Figure 9. Registered unemployed persons, number



Source: Employment Agency

12 Source: NSI, Labour Force Survey Q2 2005 figures, published 22 August 2005.

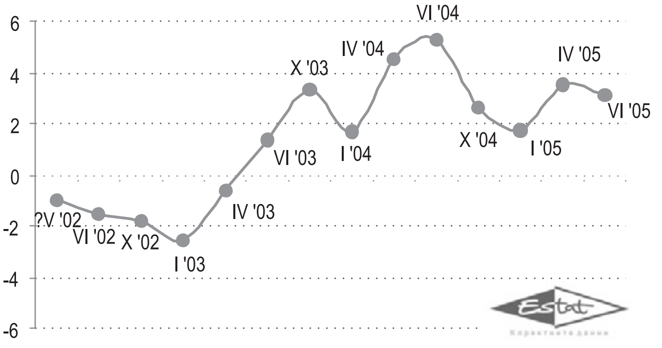
13 Economically active population consists of individuals at the age of 15 and above who employ (employed individuals) or offer their labour (unemployed individuals) in the production of goods and services.

The developments and analysis in business climate for the third quarter are presented in two aspects: based on the Estat Index of Business Climate and based on the NSI monthly business surveys; these, in spite of some methodological differences, effectively supplement each other while providing two different perspectives.

The Estat Index of Business Climate[14], July 2005.

In July, the value of the Estat Index of Business Climate in Bulgaria went down to 3.12 over its April value of 3.55. Unlike the traditional rise in optimism during summer months, the index remained almost unchanged (Figure 10) and even registered a certain decline. The political developments following the general elections at the end of June broke the usual seasonal cycles in business survey results. The lengthy and painful process of forming a government is the major reason behind the registered increase in negative opinions regarding the environment and businesses' preventively skeptical expectations. Similar feedback from entrepreneurs was also seen in the April study: then, pre-election insecurity was the determining factor behind managers' hesitant disposition. Both in April and July the following paradox emerged – the condition of companies was improving but at the same time companies' managers forecast a slow-down in development.

Figure 10. Business Climate Dynamics



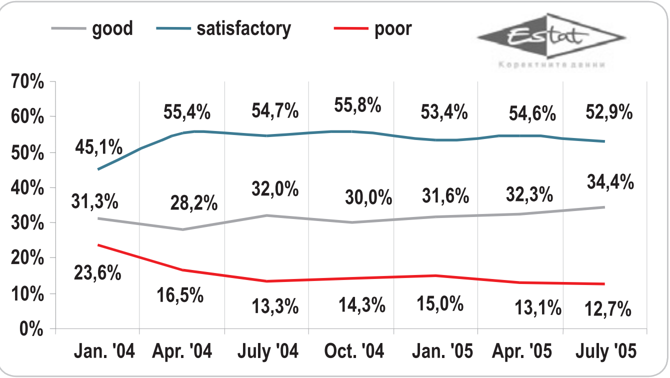
1. Company Component

In this study the component is somewhat lower in value, down to 11.32 as compared to the all-time peak registered in April 2005 - 11.95. The decline is due to lower optimism in managers in spite of the improved condition of businesses and the better resources available.

Evaluation for the business condition are going up: for the first time in the study's history the share of enterprises in "good" and "very good" condition exceeds one third of all respondents (34 per cent).

14 The survey was conducted in the period 20 July - 8 August 2005 among 400 companies and is representative at the "going concern" level. The sample criteria applied are the region, number of employees and type of ownership. The methodology behind the index and the mathematical model were developed by the Estat Agency for Social and Marketing Surveys.

Figure 11. Dynamics in the condition of businesses (January 2004 – July 2005)

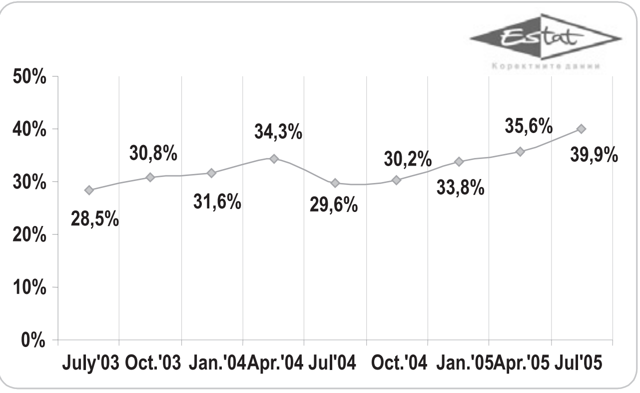


Managers associate these evaluations with the higher quality of resources available to companies. Of particular significance is the improved quality of financial resources: 58 per cent of enterprises are in "good", "very good" or "excellent" condition. For the first time since the end of 2003 such a small share of companies responding "I have no resource/financial resources" is registered: in the present study this applies to as few as 5 per cent of enterprises. The quality of computer equipment and software is also improving.

The results reveal a certain increase in conservative and precautionary approaches among managers. These are most strongly felt in defining the competitiveness of enterprises and the short-term development perspectives. This cautious approach in the business community is most easily explained by managers' apprehensions regarding possible political instability. The slow and painful process of forming the ruling majority in the newly-elected National Assembly gave rise to fears about the new government's economic policy. Some insecurity was also caused by requirements related to EU membership.

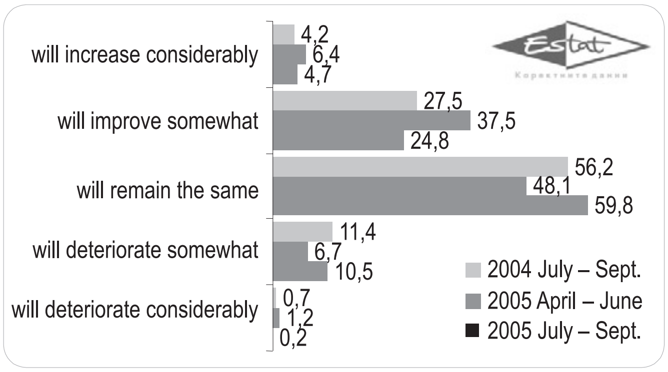
An illustration of the lower self-esteem, to a certain extent, is the fact that the share of companies declaring the absence of competitive advantages is growing – 40 per cent. This is the highest value for this index for the entire period from 2002 to the present today.

Figure 12. Share of companies without a single competitive advantage (April 2002 – July 2005)



Optimism in the short-term is sharply declining. 30 per cent of managers believe that their business will improve in the course of the next three months. The share of managers stating the same opinion in April 2005 was 44 per cent.

Figure 13. Will the condition of your business change over the next three months?

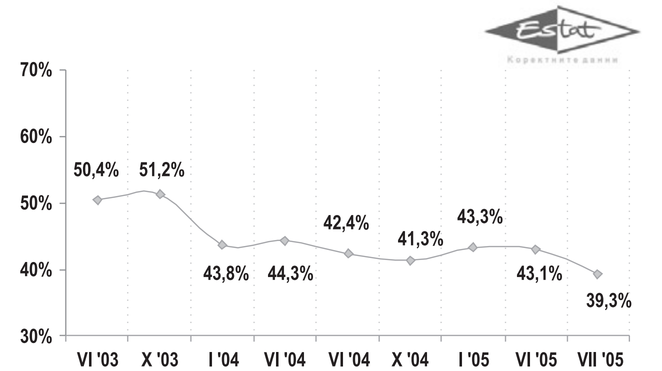


2. Investment attitudes

In July the value of this Estat index component continues to go down. Its value was 22.34 lower than the preceding value (April 2005 – 23.52) and over the same period of 2004 (29.00).

Readiness to introduce new technologies is also continuing its downward trend. The probable cause of this could be sought in the growing difficulties in personnel recruitment. Only as few as 39 per cent of managers report they are dealing effortlessly with recruitment tasks. This share registered the lowest value for the entire history of the study.

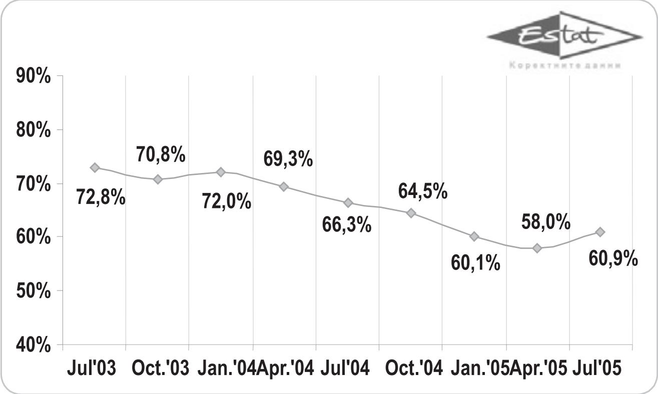
Figure 14. Share of companies agreeing to the statement "I can easily find the workers and employees I need"



An ever larger number of entrepreneurs intend to invest in new activities even if these are associated with risks. The 50 per cent share is the highest registered from April last year until today. Similar dynamics is seen with respect to intentions to use bank loans for investment purposes. Here, too, the share of 63 per cent is the highest value in studies between April 2004 and this day.

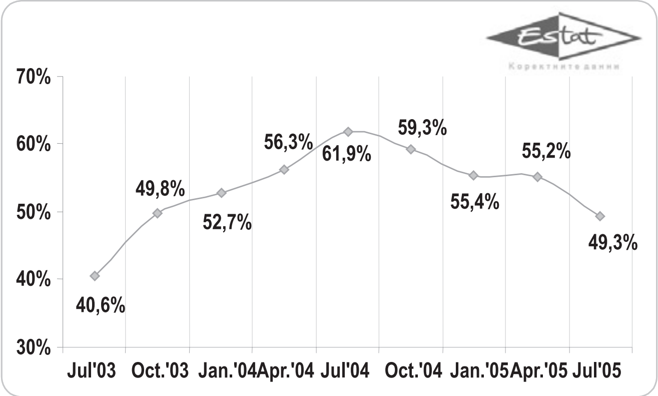
These facts give us serious ground to assume that the condition of businesses is stable. It is impossible to find a correlation between the critical condition and taking new risks in new activities, associated with drawing a bank loan, at that. To confirm this further, it is worth noting that this year the share of enterprises experiencing a shortage of financial resources is fluctuating within the narrow range between 58 per cent and 61 per cent. For 2004, the dynamics was considerably more pronounced – from 65 per cent to 72 per cent.

Figure 15. Share of companies agreeing to the statement „I experience a shortage of financial resources needed for current operations"



At the same time there has been a continuing downward trend as to confidence in the banking system; this process started during the summer of 2004. The current study reveals that 49 per cent of managers see the banking system as "stable and reliable". To compare – this share used to be 62 per cent in July of 2004. The reasons are the still very cumbersome and time-consuming procedures in granting loans to businesses (while the facilitated consumer crediting is now an undisputed fact) as well as pressure from BNB to cut down on lending which resulted in higher interest rates.

Figure 16. Share of companies agreeing to the statement „The banking system is stable and reliable"

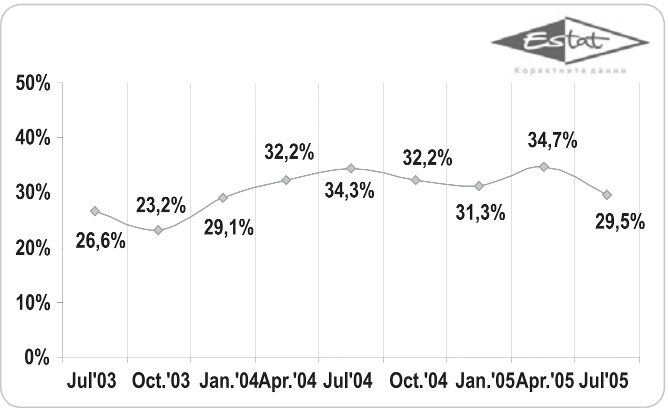


3. Environment assessment

Evaluations regarding the business environment have been changing, however slightly, in a positive direction. The value for this component has risen to -19.97, against -20.3 in April 2005.

Managers are being increasingly critical of the government policy to promote and boost business development. Discontent is also clearly visible in the area of tax policy. Criticism to the size of patent tax rates is growing. The share of those agreeing with the statement „*Profit tax is bearable to businesses*" has fallen to 29.5 per cent – the lowest value since April 2004. Meanwhile no change is registered as to the propensity to conceal income; this is based on high tax rates.

Figure 17. Share of companies agreeing to the statement „Profit tax is bearable to businesses"



The current study also registers critically low values of managers' confidence in the fairness and transparency of public procurement procedures. At the same time there has been a consistent decrease in the share of entrepreneurs who respond that administrative barriers are a major problem for businesses.

A certain increase has been registered in business community's confidence in the judiciary branch.

However conflicting these signals might seem, they have to be interpreted in the context of the recent general elections and the subsequent change of government. The highest values of fluctuation are probably marking the aspects for which managers are most expectant of changes.

Business Climate in Q3 2005, according to NSI[15]

NSI monthly business surveys also reveal signs of a slow-down in the upward trend of overall economic growth seen since the beginning of this year. For three months now the general **business climate indicator** has been going down after reaching in June its long term maximum since 1994 (35.4 per cent). In July it went down 3.5 points, another 2.3 points in August and 3.4 points in September. The September level of the overall business climate indicator is the lowest for this year.

While in July the monthly decrease was mostly due to industry (deteriorated opinion level as to the current and expected business situation) and in August due to the construction sector (more moderate expectations of the business situation) and services (slightly lower evaluation given to the current business condition), then in September the decrease is due to all sectors covered by NSI business surveys and is associated with a shift in expectations of the business condition in the course of the next six months from "better" to "the same".

Industry. In July, the composite indicator "Business Climate in Industry" went down 6.6 points (due to moderate evaluation and expectations regarding the business condition), in August it regained 3.2 points of its value (thanks to higher expectations regarding the business condition in the course of the next six months) and in September fell again by 3.7 points (due to a shift in expectations about the business condition of enterprises in the course of the next six months – from "better" to "the same").

The restraining of accelerating in industry development is shown by the year-on-year dynamics of the "Business Climate in Industry" indicator; in July it registered a downward trend for the first time since March 2003 – by 3.3 points over July 2004, in August it only slightly exceeded its value for August 2004 (by 0.1 points) and in September fell by 7.2 points over September 2004.

In July, current production activity was seen as being worse as compared to June, in August it improved over July, and August levels were preserved in September.

For the period between April and July 2005, the unutilized plant capacity went up; the average workload in industry fell to 62.2 per cent which is 2.3 points below its April level. For the same period production secured by contracted orders (measured in number of months) goes down from 5.3 to 4.8.

The situation in industry both on the domestic and export market is fluctuating – in July it deteriorated slightly while in August the level of contracted orders both for domestic and export market goes up but deteriorates again in September, particularly as regards orders placed from abroad.

Construction. Following three consecutive long-term maximum values for the past 11 years, in July the "Business Climate in Construction" indicator went down 2.1 points and then another 15.6 points in August (in both months due to a shift in expectations for the following six months from "better" to "the same" business condition of enterprises), and is stabilised

15 Source: NSI (Business Conjuncture AEAF, Recent Developments).

in September when almost 80 per cent of enterprises expect to preserve “the same” business condition in the course of the next six months.

The activity in construction has been going up throughout Q3, and in July reached its highest level for the past two years but in September continued to increases at a more moderate pace; at that time expectations about construction activity during the last quarter of the year tend to be for “preserving the same level” (78.2 per cent of enterprises).

The level of contracted construction has also been improving in the three months of Q3. Competition continues to be a major factor impeding the activity of construction enterprises (quoted by 54.6 per cent of respondents). Although it has not yet reached top position, the issue of “insufficient demand” reached in August its highest level since the beginning of this year and seems to create the highest concern among entrepreneurs.

Retail trade. The upward movement of the composite indicator “Business Climate in Retail Trade” in July and August (1.2 points and 2.5 points respectively over the previous month) stopped in September and made a down turn by 1.9 points (due to a shift in expectations for the business condition of enterprises in the course of the next six months from “better” to “the same”).
The current level in retail trade sales increased in July and August, and was preserved in September; prevalent expectations are for this level to continue throughout the fourth quarter.

A major factor impeding the activity of retail traders in Q3 was “insufficient demand”, and the “insecure economic environment” factor exceeded its long-term average value in August and continued to increase its negative impact in September, too.

Services. In July, the composite indicator “Business Climate in Services” preserved its high values but in August fell by 5.0 points (entirely due to slightly lower evaluations of the current business condition of enterprises) and by another 7.4 points in September (due to a shift in expectations for the business condition of enterprises in the course of the next six months – from “better” to “the same”.)

Current demand in services was moving up in July (5.0 points increase), preserved its level in August, and registered an increase in September when expectations for services demand during the last quarter of the year improved – keeping the same level and increase in demand (by about 55 per cent and over 35 per cent of enterprises, respectively).

During the review period, furthers steps were made towards ensuring support for entrepreneurship and improving the business environment:

- *Projects in support of entrepreneurship and SME were publicized and implemented.*
- *Business start-up was made easier with the adoption of the BULSTAT Act.*
- *An option for online form-filling in public procurement was introduced.*
- *Measures were taken towards introducing EU standards.*
- *The Bulgarian Export Insurance Agency stepped up its activity.*
- *The government announced its intentions to strengthen public-private partnerships and establish a national infrastructure.*

Nevertheless problems related to the business environment and the quality of company strategies continue to persist:

- *Entrepreneurs continue to be distrustful of the level of objectivity and transparency in public procurement which requires further upgrading of the normative base and the capacity for its implementation.*
- *Business start-up difficulties still continue thus necessitating the establishment of speedier procedures in this respect.*
- *As a whole, the new government needs to develop a strategic vision as regards the country's economic development thereby outlining priorities vis-à-vis enhanced structural reforms, including the privatisation and concessions of monopolies and infrastructure.*
- *It is possible that the limited resources of state-owned companies, the court battles over "big" privatization and concession deals and the announced intentions for a new Concessions Act will further slow down Bulgaria's structural reform.*
- *The spread of corruption practices raises serious concerns both among Bulgarian and foreign investors and policy-makers regarding the quality of the business environment in Bulgaria.*

ENTREPRENEURSHIP AND SME PROMOTION

The SME Promotion Agency continues to provide support to entrepreneurs by administering and publicising a number of projects and by expanding its activity to cover all regional cities in the country.

A good example would be the ***National Innovation Fund*** administered by the Agency as a pilot model to promote technological development and competitiveness among Bulgarian enterprises by developing and introducing innovations. The first application session for the Fund ended on 5th May, and the second one is due in October. 39 projects worth a total of BGN 16 m were approved for funding as part of the first session. Hi-tech projects prevail: instrumentation, robotics, machine-building, biotechnology.
Interest in the Fund is growing and it could become an effective mechanism to improve SME competitiveness.

Another project administered by the Agency and ME and presents a recent development is entitled ***"Support for Increasing the Competitiveness of Bulgarian Enterprises".*** As part of this project, EUR 30 m will be invested towards improving business services. The project envisages support to Bulgarian enterprises in using technical and consultant services and investing in technology. The expected outcomes include achieving compliance with the European standards and international requirements.

This project provides two ***grant schemes***: one for public-private partnership (PPP) and is targeted at municipalities and non-governmental organizations, while the second scheme is intended for SMEs of the productive sector. The first PPP scheme is to be launched in October. It has a budget of EUR 1 m, to be channeled to municipalities and business centers established in the country over the past years. The amount of individual grants will be between EUR 5 thousand and 25 thousand.

The second scheme aims to support the competitiveness of SME in the productive sector. This essentially means consultancy assistance in the process of achieving compliance with the European standards in production practices. Consultant services in evaluation and implementation of business strategies, development and implementation of marketing research, preparation and introduction of ISO will be among the activities to be financed. Obviously this is a project directly targeted at improving the quality of company strategies and operations expected to impact directly companies' competitiveness.

In August, the ME approved a list of consultants and their services, and the granting procedure for SMEs will start in October.

Currently, another ME-administered project is underway which SMEs might find particularly attractive and useful. It concerns the introduction of the cluster approach and establishing a ***pilot cluster model.*** As a result of this project, several pilot clusters will be established in selected sectors; these will then undergo institutional capacity strengthening to allow the implementation of this relatively novel approach in sectoral and regional policy.

IMPROVEMENT OF THE BUSINESS ENVIRONMENT

Company registration

Several recent developments are of major importance to improving the business environment and, above all, to enhancing

and streamlining the company registration procedures. On 10 August, ***the BULSTAT Act*** came into force. With this Act, company registers are transferred from the National Statistics Institute to the Registry Agency. Another important issue now settled by the new law is that the BULSTAT number is going to be a ***single identification number*** to replace all existing tax, social insurance and customs registration numbers.
This will beyond doubt have positive impact on the business environment and is, in essence, the practical implementation of the one-stop-shop concept. Its benefits include: stepping up the process of registration and business start-up, saving time and red tape; avoiding the doubling of documents; a smaller number of loopholes enabling corruption practices. In essence, this Act marks the beginning of applying the principle of single identification of legal entities.

It is a well-known fact that starting a business in Bulgaria, regardless of all the positive changes over the past years, continues to be a relatively challenging process giving rise to entrepreneurs' deserved discontent. Business start-up procedures take about 30 days which is almost twice the target time-limit for EU countries adopted by the European Commission (18 days).

Self-employed individuals or craftsmen and other natural persons who are social insurance payers must be registered by 11 November (three months after the law's entry into force). Persons and entities registered under the former procedure have no obligation to re-register. All registered entities however will be obliged to report to the Registry Agency within 7 days of any change in the data contained in the registration documents (f.e. change in the company's business address). For joint stock companies, a notification of change will only be mandatory if the change of ownership by separate shareholders exceeds 10 per cent of the company's capital.

Those failing to meet the law's requirements are liable to sanctions up to BGN 700 for natural persons and up to BGN 1000 for legal entities and sole-proprietor merchants.

The size of fees remains unchanged. A new requirement is that fees will not be paid in cash at the desk; all fees must be paid by a bank transfer to the Registry Agency's account. Companies and individuals will be issued with a registration certificate containing the BULSTAT code which is for temporary use only, pending the issue of the identification card, and will expire in one month.

Currently, the new Act does not release companies from other registration procedures – at the National Social Insurance Institute and Tax Offices. The law specifies that Tax ID numbers will only be valid until 11 February 2006. Following this date, the data exchange between the BULSTAT Register and the Tax Register will be performed through the proper official channels.

The BULSTAT Act, now adopted and in force, is a major step towards facilitating business start-up in Bulgaria. The next steps in this direction would be: introducing lower registration fees; an option for online filling-in and filing of BULSTAT Register applications; transferring companies' court registration to the Registry Agency; online access to information in the BULSTAT Register etc.

The adoption of the BULSTAT Act is a milestone in the process of reform in company registration and the establishment of an electronic registry center[16].

There are four stages in the implementation of the strategy objectives:

1. Establishing a Central Register of Legal Entities.
2. Establishing an Electronic Registry Center.
3. Merging tax registers, vehicles registration, ESGRAON etc.
4. Establishing a central real property register.

Public procurement

Entrepreneurs' opinion on the objectivity and transparency in public procurement continues to be on the negative side.
Early October marked one year since the entry into force of the new Public Procurement Act (PPA). Regretfully, there is still no positive change in the opinion of the business community and its branch associations as to public procurement procedures. Once again the "Estat" Agency business climate surveys register a very small share (as few as 8 per cent) of respondents saying that PPA tenders are transparent and fair. Obviously measures must be taken towards more strict adherence to legislation governing the public procurement procedures and further upgrading of the PPA. There is still no information on progress achieved in preparing the amendments to this law by the inter-ministerial group; the European Commission has repeatedly requested such amendments.

Some changes have been applied to the normative base during the review period, and steps were taken to ease public procurement procedures.

In July the government adopted changes to Regulations on Implementation of the Public Procurement Act. By these changes, contracting authorities for public procurement which are public-law organisations will be allowed to award public procurement under a simplified procedure established for sectoral contracting authority, but only for communal activities[17].

An important achievement towards greater transparency in procedures is that since early August ***the Public Procurement***

16 The former government approved a Strategy for Establishing an Electronic Registry Center.

17 Changes are discussed in greater detail under the "Legislative Changes in Economy" section of this report.

Register(PPR) provides a new service: ***online filing of tender notice forms***. It will be accessible to contracting authorities having a universal electronic signature and are authorised users. The Public Procurement Agency webpage provides step-by-step instructions on how to register as an authorised user.

The number of contracting authorities owning a universal electronic signature is still quite small. Therefore the price cuts for e-signatures announced by the two suppliers of certification services – "BankService" AD and "Information Services" AD, earlier this year will contribute towards the wider use of this new service.

The online filing of tender notices in public procurement circumvents the need to send documentation in paper form. This saves time and money both for contracting authorities and for experts maintaining the PPR. The risk of technical errors is also greatly reduced.

PREPARATION FOR THE SINGLE EUROPEAN MARKET

With the ever closer full EU membership of Bulgaria, issues related to the preparedness of Bulgarian companies to cope with the competitive pressure of the EU market become increasingly pressing.

Adopting EU standards is very important in this respect. As legislators' attention shifted towards the general elections, the difficult task of forming a new government and the need to catch-up with the delayed transposition of the acquis, the adoption of EU standards was increasingly delegated to public administration offices, branch organisations and individual companies. In milk-processing industry for instance efforts were focused on support to enterprises in introducing the Hazard Analysis of Critical Control Points system – HACCP. The goal is for Bulgarian companies to organise their production process in a manner that allows ongoing control at every stage of the process. Thus responsibility for product quality is taken entirely by producers and the involvement of the state is limited. As of yet, only 10 per cent of enterprises are EU certified. As part of the implementation of the second stage of the project by the Ministry of Economy and Energy, 79 milk-processing enterprises will receive funding; these were screened for eligibility and have the capacity to produce successfully for the European market after certification.

TRADE POLICY

In implementation of Bulgaria's pre-accession commitments, the government took steps to achieve compliance with the acquis of the country's international treaties. This involves denouncing or modifying tens of bilateral agreements on trade and economic co-operation: free trade agreements, investment agreements etc. These treaties and agreements regulate Bulgarian trade policy, while, pursuant to article 133 of the EC Treaty, matters of trade policy are exclusively within the competence of the Community. The majority of these agreements contain provisions on termination by mutual consent or denunciation as they can easily be replaced by the relevant EU agreements. However, some agreements that cannot be regulated by the acquis, will have to be negotiated for amendment or termination in case no agreement is reached by the date of accession.

Measures aiming to strengthen the role and importance of the **Bulgarian Export Insurance Agency (BEIA)** and thus create export incentives are already yielding results. The Agency's insurance capacity was increased this year and the insurance limit covered by the state is now higher. As a result of the improved activity in export insurance, the Agency's revenues for the first half of the year are now nearing last year's total revenues. Three-thirds of the entire premium revenue is from insurance policies made at the expense of BEIA itself, and only one third – from insurance policies covered by the state. This is mostly associated with export destinations as most of it goes to low-risk countries and so insurance is covered by the Agency. The gradual increase in exports and the normalisation of the export process BEIA activities are expected to expand.

PRIVATIZATION

One of the factors largely negating the positive evaluation given to Bulgaria's microeconomic stability are entrepreneurs' opinions on the state of infrastructure and its negative impact on business environment. Available data on the state of the Bulgarian economy and its growth potential would logically lead to recommendations on accelerating ***structural reforms in the country***. Currently, Bulgarian economy is largely in the hands of private investors while the state continues to hold the monopoly over road Infrastructure, railway transport, district heating, and (partially) on power generation, gas supply and electric power supply.

The new Bulgarian coalition government needs to adopt a strategy for the development of Bulgarian economy and state its intentions on the privatisation and concessions of monopolies and infrastructure. Such a programme is further necessitated by the fact that the pre-election programs of political parties which are now coalition partners are to a large degree in disagreement vis-à-vis the state's involvement in managing property and infrastructure. Centrist parties stood for the withdrawal of the state through privatisation and concessions of infrastructural facilities, while leftist parties agreed to structural reforms but on condition that state ownership is preserved.

The heritage from: 1) the failed sales of state-owned companies ("Bulgartabac Holding", "ADIS"); 2) legal disputes (Bulgarian River Shipping, Bobovdol Mines); 3) privatisation strategies that the National Assembly failed to adopt: Navigation Maritime Bulgare, Bulgaria Air, the VMZ military plant; 4) the postponed sales of defense industry companies Kintex and Teraton as well as the absence of government support to the development of the capital market, leave no doubt about the hard times to be expected in Bulgarian privatisation.

According to figures supplied by the Privatisation Agency of 21 September 2005, the state holds majority interest in 63 commercial companies. Most of them are in the construction and energy sectors. Another 113 companies in which the state holds majority interest were included in the so called “prohibited list” annexed to the Privatisation and Post-Privatisation Control Act.
Minority state interest is still preserved in 519 companies, of which 301 share packages are intended for satisfying restitution claims.

Since January 2005, the Privatisation Agency has concluded privatization deals for 29 companies with majority state interest, 8 autonomous parts and 193 sales of packages/shares in commercial companies with state interest below 50 per cent.

The group of companies now being prepared for sale by PA in the Energy sector includes 10 HPPs, autonomous parts of NEC EAD, the district heating companies in Plovdiv, Shumen, Pernik, Varna and Sliven.

Negotiations on the sale of CHPP “Rousse” EAD and CHPP “Varna” EAD with the winning bidder, RAO EES Rosiyi, are drawing to a close. The Commission on the Protection of Competition issued a decision banning the Russian company from acquiring both companies. CPC motivated its decision by stating that the purchase of both companies will cut down on competition in the sector will have negative impact on the sector. In support of this opinion comes the expert appraisal that, following the decommissioning of units Three and Four of Kozloduy NPP the influence of private companies connected to the power grid will grow.

The privatisation of hospitals which started under Ivan Kostov’s government was discontinued by the NMSII – MRF coalition. Socialists in the former National Assembly also spoke against the privatisation of healthcare facilities. The new health Minister, a Bulgarian Socialist Party representative, announced that within a year a privatisation procedure will start for hospitals and outpatient care centers, with preference given to doctors working in these hospitals. A privatisation moratorium will only be imposed on university hospitals.

CONCESSIONS

The government stated its intention to improve the national infrastructure by ***applying public-private partnerships*** and attracting private capital at the expense of centralised government funding. This is the most serious challenge in awarding concessions of public state property. According to experts and government officials, the current Concessions Act does not reflect the actual economic situation and the country’s EU commitments on establishing real market competition in concessions. The direct award of concessions with the privatisation of state-owned companies and the attracting foreign investment through the establishment of joint ventures meets no support from the European Commission. Some remarks were also addressed to the acquis implementation in concessions legislation. This calls for a ***new Concessions Act*** to introduce the *acquis* principles of free competition, and the specific requirements Directive 2004/17/EC on public procurement and Directive 2004/18/EC on the award of public works. The government’s intentions are that the principles of transparency should be in place from the stage of announcing the contest, through the Concessions Register and to the final selection of the concessionaire.

Airports

The Supreme Administrative Court issued a decision in October on the case regarding the disputed winner in the concession award for Varna and Bourgas airports. The legal procedure was initiated by the applicants ranked second and third: the Bulgarian/German consortium Fraport AG/BM Star and the French Vinci Airports/Vinci Concessions. The winner selected by the contest commission, “Copenhagen Airports”, is prepared to invest EUR 140 million in the next three years after the award of the concession. The investment will be needed for the expansion and modernisation of the two airports as they are now struggling with the increased inflow of tourists, and to ensure a high quality of services.

The future of a possible concession of two other Bulgarian airports – Rousse and Gorna Oryahovitsa, is still very uncertain. The new Minister of Transport stated his opinion there was no need to start an accelerated concession procedure for Gorna Oryahovitsa Airport – the fifth international Bulgarian airport. The airport is used for charter, cargo and passenger flights, as well as for import and export of industrial and agricultural goods.

Ports

Following the Constitutional Court decision of 10 May 2005 on the authority of the newly established Ports state company, the current and future concessionaires of Bulgarian ports will continue to report to the Port Administration Executive Agency. This is stipulated in Ordinance № 9 of the Ministry of Transport and Communications. The Ordinance only applies to public transport ports.

The concession procedure for the Danube terminal Oryahovo, part of the port for public transport Lom (public state property), is now underway. Two companies were admitted to participation in the one-tier contest: the Bulgarian “Slanchev Dar” and the company G.E.K. S.A, registered in Greece. The contest requirements include investments of at least BGN 291 thousand for the first two years of concession.

The Slanchev Dar company is also bidding for the concession of the Svishtov Port, part of port for public transport Rousse, together with the Dragajen Flot Istar and Interport companies. The winner in the contest is expected to be announced in October.

Bidders for the concession of the Balchik port terminal, the companies Port Balchik, Himimport Balchik and Papas Port, filed their bidding offers to the commission on 12 September 2005.

Three companies were admitted for participation in the concession procedure for a period of 35 years of the Silistra ferry terminal. The terminal is a territorially separate part of the Rousse Port for Public Transport and was declared a site of national significance. Companies admitted for participation include Mineral In, "Ferry-boat Complex Silistra-Calarasi - Bulgaria" and "Himimport"

Two companies took part in the one-tier non-attendance tender announced by the Ministry of Transport for award of concession for a period of 35 years of the port terminal Vidin-South: "Vidahim" and "Bulgarian River Shipping". Bids are expected by 31 October 2005.

Construction materials

The Council of Ministers, upon proposal by the Ministry of Environment and the Ministy of Regional Development issued permits to seven companies for prospecting of mineral resources used as construction materials.

About BGN 200 thousand will be invested in research and prospecting of construction materials, and BGN 21,116 are earmarked for environmental protection activities.

The company PSI was awarded concession for a period of 35 years for the construction materials deposit Vinarovo, Chirpan municipality, Stara Zagora Region.

Almost BGN 70 thousand will be invested in research and prospecting of tiling materials in the Vlashko Selishte area, Vratsa Region, by the "Hemus-M." company for a peroid of two years.

Coastal Beach

A Council of Ministers' Decision of September 2005 named the concessionaires of three coastal beach strips on the Black Sea in the municipalities of Kavarna, Balchik and Bourgas. The concession is awarded for a period of 15 years and expected investments are in the amount of BGN 6 m. Investment programs envisage sports and entertainment activities, securing public order in the area, provision of medical services to visitors and adjustments to accommodate the environment for use by disabled people.

Oil and Gas

The Pleven company "Oil and Gas Exploration and Extraction" was granted authorisation by the Council of Ministers to undertake oil and gas exploration in Shabla block of the northern Black Sea shelf, on an area of 2,776 sq. km. The company will invest over BGN 7 m, and will pay BGN 83,280 per year in area fees.

The Russian company OAO Bashkirgeologia will prospect for oil and gas in the Yambol block, Southeast Bulgaria. Initial investments will be in the amount of BGN 8 m, and the area fee will be BGN 120,150 per year.

With these decisions in effect the entire land and water territory has been awarded under concession for exploration and prospecting of oil and gas.

The Ministry of Environment and Water divided the deep-sea section of the Bulgarian sea economic area into two parts – "Varna Deep Sea" and "Bourgas Deep Sea". The Austrian OMV company and the American Vintage company are prospecting there. The central, part of the northern and the entire southern shelf are developed by Petreco; this company is already extracting gas from the Galata Cape shelf and selling it to Bulgargas. The American company is currently researching opportunities for methane extraction in the Dobrudja coal basin, and the US company Anschutz operates one of the largest land blocks, A-Lovech.

FIGHT AGAINST CORRUPTION

The spread of corruption practices negatively impacts business environment and the economic growth potential.

In a ***Report on global competitiveness 2005-2006*** by the World Economic Forum published late in September, Bulgaria was ranked 38th in corruption practices, which means a deteriorated position as compared to previous years (30-th position in last year's report). This is a clear signal from the business community on the severity of the corruption issue. At the same time, in a business climate study carried out by the "Estat" Agency in July, about 80 per cent of respondents replied that they were prepared to pay more money to avoid difficulties with the administration.

Senior EU officials, Heads of State, Ministers from Member States, ambassadors, and scientists have been warning for a long time in one form or another that the problem with corruption might pose one of the most serious barriers to Bulgaria's EU accession. Similar messages have also come from the IMF, the World Bank and other international organizations. Businesspeople in the EU also believe that Bulgaria needs to make major efforts in the fight against corruption and red tape[18].

The new government announced that one of its priorities will be the fight against crime and corruption. A Code of Conduct for Ministers and members of political cabinets in the executive branch is now being drafted and will soon be published. The document is part of the implementation of the National Strategy against Corruption, which in February was further expanded by the former government to include a new section envisaging anti-corruption measures "at the top".

The Anti-Corruption Coordination Commission headed by the Minister of Justice, is preparing a report on the implementation of the National Strategy Against Corruption In parallel to this, a new programme for 2006 is being drafted to educate civil servants on issues related to professional ethics and counteraction and prevention of corruption[19].

Public announcements of the intention to step up the activity of the parliamentary Commission against Corruption were also made. The Commission's main tasks include: review of current legislation and proposals for amendments to laws establishing settings and conditions that favour corruption; parliamentary control at the Commission level, to be used as a sort of prevention measure on corruption alerts filed to the Commission; special commitment for efforts by the commission on cases of social significance, within its authority.

The initiative taken up by the Supreme Prosecutor's Office of Cassation (SPOC), is of particular interest. A working group of prosecutors at SPOC drafted a set of measures for fight against corruption in various fields and proposals for amendments to five laws: the Privatisation and Post-Privatisation Control Act, the Concessions Act, the Public Procurement Act, the Municipal Property Act and the State Property Act. These proposals were submitted to the Commission for fight against corruption at the National Assembly. Anti-corruption measures are part of prosecutors' experience in their work on operational files and legal cases for fraud involving state property.

Bulgaria stated her readiness to take up the fight against corruption and with the signing of the UN Convention against Corruption in December, 2003 On 15 September 2005 this Convention received its required 30th ratification and will come into force in December. The Bulgarian Parliament will also ratify the document. Although that of all G-8 countries only France has ratified the Convention, it is still an important serious tool in the fight against corruption, including the restoration of funds appropriated by dictators; increasing pressure on banking institutions to take stronger measures against money laundering; facilitating judicial cooperation on the international scale etc.[20]

Without any doubt, these and other ideas and initiatives will be completely useless if there exists no systematic and steadfast political will on their practical implementation. Meanwhile experience shows that anti-corruption efforts can only succeed if they are implemented in parallel and in cooperation between authorities at all levels and civil society structures.

OVERALL ASSESSMENT OF BULGARIA'S POTENTIAL FOR ECONOMIC DEVELOPMENT AND ENTREPRENEURSHIP

(Bulgaria in reports by the World Economic Forum, the World Bank and UNDP)

Over the past months, the reports of several international organizations containing analyses and assessment of countries' business environment and economic potential were published; Bulgaria is also mentioned in these reports. Such evaluations are important for setting the development direction of Bulgarian business and entrepreneurship.

In September, the new report of the ***World Economic Forum on Global Competitiveness*** was published. It contains a summarised assessment of both the competitiveness of national economy and of enterprises' capacity to cope with the competitive pressure of market forces.

Bulgaria is part of the report for the 7th year in a row. In 2005, the country moved up ***one position in the global ranking: from 59-th to 58-th place***.

Bulgaria improved its position vis-à-vis ***microeconomic stability*** the country now goes up from 54th to 51st position. The score this year is lower, however, as concerns business people's opinion with regard to the quality of public institutions. This is mostly because of the deteriorated assessment on the functioning of the judiciary branch (88th place among 117 countries). Also negative are the results on organised crime and property rights protection.

Traditionally, in World Economic Forum reports Bulgaria scores well on ***prevalence of corruption*** – over the past several years the country usually hovered around the 30th position. In the latest report, however, there is a step back and now Bulgaria is ranked 38-th.

Bulgaria features a relatively good position with respect to ***the Technology Index***. The evaluation on technology transfer and innovation (58th position over 62nd last year). Looking at ***quantitative indicators,*** Bulgaria shows good results

18 http://www.evroportal.bg/print.phtml?tid=40&oid=727066

19 http://www/online.bg/asp/s3nArt.asp?media=54&artno=15&ardate=2005/9/16&CDLANG=BG

20 http://www.transparency-bg.org/?magic=0.5.87

for: number of telephone lines, per cent of people at higher education establishments; number of Internet users; number of Internet hosts.
The business community gives a negative assessment to the state of research and development activities, the cooperation between university centers and businesses, the insufficient role of foreign investment in the introduction of new production technologies.

Bulgaria continues to score poorly as regards ***business competitiveness*** in two of its basic components – company strategies and business environment. This casts serious doubt over the preparedness of Bulgarian companies to cope successfully with the EU competitive pressure.

The quality if education in natural sciences and mathematics and the presence of well qualified technical professionals is given a relatively high evaluation; these factors set favourable grounds for companies' innovative development.
Bulgarian infrastructure gets a low score and is seen as a barrier to successful business development.
As regards ***company strategies***, of note is the lack of experience and professionalism in company management as well as the absence of active training and career development policies.

Indicators on which Bulgaria scores relatively high include: labour market flexibility; productivity/wage ratio; equal opportunities for women on the labour market; access to loans. Problems are reported in environmental protection and preserving the environmental balance.
As a whole however the country's positions as regards national competitiveness are moving up, although slightly.

Another important paper assessing the business environment and entrepreneurship was also published in September; it is the World Bank report entitled ***"Doing Business in 2006: Creating Jobs"***. It contains a country rating on the "ease of doing business". Among the 155 countries ranked, Bulgaria occupies 62nd position. New Zealand tops the ranking for business-favourable environment. Analysts observe the greatest improvement in business conditions over the past years in Serbia and Montenegro, Romania, Latvia, Slovakia etc.

Data on Bulgaria says that 11 steps have to be taken to start a new business, which takes about 32 days on average. In OECD countries, the number of steps is equal to 6 and respectively it takes an average of 19 days to start a new business. New business registration expenses amount to 9.6 per cent of the gross national per capita income, while it is 6.5 per cent in OECD.

The number of tax payments made by businesses in Bulgaria, is 27, while it is 16 in OECD. The time needed to pay tax in Bulgaria equals to 616 hours over 192 in OECD countries.

These figures re-confirm the need to apply additional measures for improvement of the business environment. Changes in company registration effected through the BULSTAT Act are undoubtedly a good solution that will probably cut down significantly on the time and financial resources needed.

In the course of the past month **the annual UNDP Human Development Report** was published. Bulgaria now occupies 55th position which means several positions up in the ranking. The base of the report's rating and analysis is the Human Development Index and its three basic components: life expectancy, income, education. The report notes that inequality in in individual countries, including in Bulgaria, reduces the effect of economic growth on battling poverty. This means that it is necessary to create an environment in which poor people could increase their share in the future growth of national income.

European entrepreneurs on the business environment in Bulgaria

Of genuine interest for the state of business environment is the ***opinion of European businessmen*** presented in a special position paper by the Union of Industrial and Employers' Confederations of Europe on Bulgaria's progress towards EU accession. As a whole, the reforms in the country are positively evaluated. More specifically this concerns:

- successful adherence to macro-economic stability;
- good results and rates in conducting reforms;
- clear EU membership prospects;
- improvement of the investment climate;
- implementation of the acquis in business.

European investors are most attracted by: access to a market developing at a rate faster than the EU average; expected financial inflow from EU funds; continuing harmonization and upgrading of implementing legislation; flexible labour market; relatively low personnel costs and tax rates; relatively well-qualified workforce; access to loans; low corporate tax rates.

At the same time, European businessmen ***criticize*** and call for measures with respect to:

- reducing corruption;
- downsizing the "grey" economy;
- removing red tape and administrative barriers to businesses;
- stepping up executive proceedings;
- improving infrastructure;
- improving transparency in public procurement.

Recent developments in public finance are characterized by the persistence of major trends started in previous periods, among which the presence of chronic budget surpluses and the reduction of foreign government debt. The new government proposed a set of measures to reduce the tax and social insurance burden; these however achieve not a decrease but rather the re-allocation of the burden from direct to indirect taxes.

Budget execution as of the end of August 2005

Consolidated Budget[21]. At the end of August came the now traditional reports on the considerable over-execution under the consolidated fiscal program. According to figures by the Ministry of Finance *the surplus* under this program reached BGN 1 318.2 m.

Table 3. Budget surplus/deficit for the respective year (in million BGN)

	Date		
	31 August 2003	31 august, 2004	31 august, 2005
Amount	729.1	1,191.6	1,318.2

Source: Ministry of Finance, “Budget” bulletin

Comparing figures for the first eight months of three consecutive years we can now confirm that at the end of 2005, if the growth trend is preserved, the budget surplus will move closer to our forecast made end- 2004 of a budget surplus of about BGN 2,000 m for 2005. That is, about BGN 2,000 m more will be collected from individuals and enterprises and will be transferred under the disposal of public authorities in a manner not stipulated in the State Budget Act estimates. If, instead of being expropriated from businesses, these substantial resources had been put to use by taxpayers for consumption and investments, Bulgaria’s economic growth would have been more intensive. While the policy of circumventing the Budget Act was gaining momentum in 2003, in 2004 and particularly in 2005 it reached a climax. It is our hope that the new Ministry of Finance, and the new government, respectively, will discontinue this vicious practice and thus introduce a transparent governance style as regards the state’s financial matters, as it promised: zero budget deficit and expenditures and revenues of no more than 40 per cent percent of GDP.

Revenues and aids as at end-August reached BGN 11,758.6 m. i.e. a 14 per cent increase over the end of August last year. The good rate of execution of the revenue side, as in the preceding period, is entirely due to the good collection rate for tax and non-tax revenues.

Expenditures for the same period registered a growth of 14.5 per cent over August last year and reached BGN 10,440.5 m. The largest relative share in the composition of consolidated expenditures is attributed to: the national budget22 – 41.4 per cent, social insurance budgets – 34.5 per cent, and municipalities’ budgets – 15.1 per cent.

Budget 2005, in spite of the declared steps towards applying the so called program budgeting, does not reflect the priority goal, which is accelerated economic growth. We are now expecting Budget 2006, which, together with the amendments to tax legislation, will be submitted by the government to the National Assembly by end October.

The pre-election promises of the ruling coalition contain no indication of a more targeted and efficient management of government finance in the years to come. A positive sign in this direction is the personality of the new Finance Minister, Mr. Oresharski, and the external pressure and control on the part of European Union and international financial institutions.

Fiscal reserve[23]. The upward trend for the fiscal reserve since February persisted through June. In July, at the very end of the term of office of the former government, it went down by BGN 615.4 m and as at end-August reached BGN 4,646.6 m. The decrease in the fiscal reserve in July coincided with the reduction of foreign debt by EUR 518.1 m in the same month. Within the structure of the reserve, at end-August the accumulated funds in BNB deposits reached BGN 4,101 m, and these in foreign currency deposits reached BGN 1,967.1 m.

A weakness in the former government’s work was that it did not succeed in drafting an economic concept and its pertaining legal framework on the use of the fiscal reserve. It is our wish for this practice to be discontinued so that in the future Bulgarian taxpayer’s money can be reallocated through the budget, and not in a concealed, off-the-book manner.

There is a **surplus** in the amount of BGN 1,198.9 m in the *national budget* for this period. Revenues and aids account for BGN 7,779.6 m., while expenses and transfers amount to BGN 6,581 m. Revenues are mostly generated from tax proceeds while expenditures consist mostly of running costs of and interest payments. As of end-August 2005, **municipal budgets** also registered a proforma surplus in the amount of BGN 66.9 m calculated as the difference between revenues – BGN 591.9 m and net transfers – BGN 1,057.3 m, on the one hand, and expenditures – BGN 1 582.4 m, on the other.

21 The consolidated budget covers the national budget and all autonomous budgets – those of local governments, social insurance funds, state universities, Bulgarian Academy of Science, Bulgarian National Radio, Bulgarian National Television, Supreme Judicial Council, as well as extra-budgetary funds and accounts on central and local level.

22 Comprising the central budget, budgets of ministries and agencies and the budget of the Audit Office.

23 Covers cash in BGN and foreign currency on all current and term deposits with the BNB and commercial banks of the central budget, the budget funds of ministries and agencies, the National Social Security Institute, the National Health Insurance Fund and their extra-budgetary accounts and funds, as well as other high- liquid low-risk financial assets in foreign currency of the government.

In view of the central role of the national budget within the structure of the consolidated fiscal program, a more detailed analysis of its revenue and expenditure sides is necessary.

Revenue side of the national budget

Tax revenues to the national budget as at 31 August, 2005 amount to BGN 6 337.6 m, which means a 72 per cent execution of State Budget Act estimates.

The largest share of tax revenues is that of **VAT** – 38.6 per cent of total revenues and 47.4 per cent of tax revenues. As of end-August, an execution of 70.9 per cent was registered for this type of tax over the Budget 2005 estimates. VAT collection rate is improving, which is mostly explained by:

- the improved control exercised by the tax administration in VAT collection;
- the legal procedures initiated for VAT-related tax fraud, VAT chains, ghost companies etc.

A major problem, leading to companies trying to circumvent VAT, is the slow tax credit refund. The inability to solve this administrative situation in combination with the high VAT rate considerably deteriorates companies' liquidity. Import, export and domestic trade are also made costlier. Businesses either pay with very expensive working capital loans, or respond by setting up illegal trade chains evading VAT, and then (as they are forced to) also avoid paying corporate tax.

The excise duty and charges on liquid fuels as at end-August reached BGN 1,368 m. They also feature a high relative share of total revenues – 17.6 per cent, and 21.6 per cent of tax revenues, with both shares slightly up over the previous quarter. As to excise duty, an execution of 70.3 per cent was reported as at 31 August.

Personal income tax as at 31 August has a relative share of 10.6 per cent of total revenues and 12.9 per cent of tax revenues. An 67.2 per cent execution of budget estimates is registered; the amount in absolute terms reached BGN 817 m.

Corporate tax. The share corporate tax revenues for the period is 9.3 per cent of total revenues and 11.4 per cent of tax revenues, and in absolute terms it reached the amount of BGN 722.7 m. The corporate tax execution as compared to budget estimates is 79 per cent, which clearly shows the limited scope of tax breaks introduced earlier this; more so because for this type precisely there are number of legal provisions that would allow tax cuts. The rate of execution of proves in practice the conclusion that if the tax rate is cut below the psychological barrier of 10 per cent, the share of taxpayers who would “come out in the open” and file tax returns showing their real profit, would increase considerably.

Duty tax. Revenues from duty tax and customs charges as at end-August are in the amount of BGN 230.9 m, which means an execution of 96.2 per cent and a 2.9 per cent share in total revenues. The considerable execution of budget estimates is mostly due to the growing imports and the improved work of customs administration.

Dividend and income tax. Revenues from this are in the amount of BGN 63.4 m, thus registering a 104.4 per cent execution. This result clearly shows that the tax cut from 15 per cent to 7 per cent is negligible in size. Both economic and fiscal analysis reveal that dividend tax must be done away with; this, combined with the gradual cuts in corporate tax, will result in a tax environment creating strong incentives for businesses and boost foreign investment.

Non-tax revenues to the national budget reached as at 31 August the amount of BGN 1 419.6 m, which is 87.2 per cent of Budget 2005 estimates. The amount of state fees is to be given special attention; its execution is 123.8 per cent only for the first eight months of the year. It is obvious that if most of them are to be removed, the budget, although very generous in this part, will still be over-executed. The large number of fees and charges, alongside red-tape and corruption, are a major barrier to businesses in Bulgaria.

Expenditures side of the national budget

Gross Expenditures. Expenditures by end-May amount to BGN 4,323.1 m, over BGN 3,789.7 m for the same period of last year, thus registering a 14 per cent growth.

Running costs. With a relative share of 40.4 per cent of total expenditures as at 31 August, running costs amount to BGN 1,746.3 m. These incorporate expenditures for medications, fuel, energy, hired services, current repair, and also defense and security expenditures. The expenditure made for this period represent 61.7 per cent of expenditures planned for 2005.

Interest. Due interest on foreign and domestic loans is also a point of focus. As at end-August these amount to BGN 599.2 m (BGN 445.9 m on foreign and BGN 153.3 m on domestic loans).

Social expenditures and scholarships, now in the amount of BGN 426.5 m register an execution of 50.6 per cent against budget estimates.

Subsidy. With regard to subsidy, there is a 7 per cent growth over the same period of 2004. As of end-August 2005, these amount to BGN 430 m, which means 78.2 per cent of budget estimates.

Net Transfers. Net Transfers., i.e. the difference between transfers made and received from the national budget, reached BGN 2,257.6 m and register an execution of 68.3 per cent.

Foreign and domestic debt

General government debt. As of end-August, the size of government and government-guaranteed debt reached EUR 5,483.6 m in nominal terms, which is EUR 570.7 m less than the end-of-May figures.

Domestic debt. For the period between end-May to end-August, domestic debt increased by EUR 13.6 m, reaching EUR 1,428.9 m.

Foreign debt. As of end-August, foreign debt amounts to EUR 5,483.6 m, which means EUR 584.3 m less over the end-of-May levels; notably, it lost EUR 518.1 of its value only during the month of July.

Debt/GDP. The Debt/GDP ratio as at end-August is 32.7 per cent registering a decrease over its end-of-May values by 2.7 percentage points.

When drafting Budget 2005, policy-makers announced that it will be in line with the country's top priorities: (1) long term economic growth; (2) tax cuts for key tax; (3) income growth; (4) efficient use of budget expenditures and others. These announcements only partially reflect what was actually achieved during the first 8 months of this year.

It is a fact that Bulgarian GDP is growing but the growth rate is much below what is actually achievable by the Bulgarian economy. Tax cuts were indeed effected in 2004, but this measure came much too late and was too limited in size to ensure the intensive growth of economy and incomes.

If one is to seek the results of "priority" expenditures according to Budget 2005 in areas such as health, defense and security and the judicial system, one would find that the enormous public discontent with the health system continues to grow, and the problems of the judiciary branch and national security are still the object of severe criticism and a major barrier to Bulgaria's EU accession. Outside these priorities, there are no economically convincing development strategies for key areas - education, for instance. Bulgarian infrastructure is still in a dire state condition and serves to discourage foreign investors. The quality of services, provided by the over-staffed administration continues to be very poor in spite of the enormous expenses.

Fiscal policy – the new government's touchstone

Promises of financial benefits were abundant at the time of 2005 general elections. With regard to transfers of the "Christmas benefits in the budget-financed sphere, higher pensions etc." BSP was the undisputed leader although the party was simultaneously targeting a 40 per cent revenue re-allocation through the budget. Through personal income tax, socialists wanted higher rates imposed on the rich; this was however to be set-off by a zero tax rate on reinvested profit, and for some of them, in sectors declared as priority by the BSP, some tax breaks were contemplated. The second coalition partner in the current government, NMSII made its pre-election profile mostly with a set of new tax laws, the unfortunate product of Bulgarian tax officials. MRF left tax policy in general to "the big ones" and focused mostly on EU funds absorption. Everyone was in support of the idea to reduce VAT from 20 to 18 per cent.

Coalition negotiations served to clear away some of the more striking populist components, although intentions for VAT cuts to 18 per cent still persist. The socialists agreed to cut the limits of brackets for personal income taxation, and consensus was reached on profit tax.

Unlike the uneventful management of government finance and with focus mostly being on foreign debt transactions (the effect of which is mostly very negative) by the former government, the new government's start was marked by money-consuming shocks and disasters: floods, sky-rocketing oil prices, pressure to deliver on populist promises. Another encumbrance was the delayed reform, including reform related to the structure of the revenue financial system and administration. In addition, the political base of the new government on fiscal policy seems rather shaky, taking into account the difficult coalition talks. Nevertheless changes in the fiscal area are needed not only in execution of pre-election platforms but also because of the enormous gaps in this key area of economy.

The major problem areas in fiscal policy are six, at a minimum: (1) cutting down on government spending, (2) restructuring and upgrading of the revenue collection system (tax, charges, social insurance contributions etc.), (3) upgrading the substantive law base of the tax system, (4) upgrading and introducing a fiscal decentralization system, (5) reducing the overall tax and social insurance burden based on a substantiated economic concept, and (6) putting an end to the attempts for budget surplus spending that is not sanctioned by the Parliament.

On this background, we will proceed to explain each of these problem areas in some greater detail.

(1) It is usual for countries registering considerable economic growth to have a low share of resource allocation through the budget (about 30-37 per cent). Coalition partners agreed on a share of 40 per cent for re-allocation, as was promised during the election campaign, thus clearly indicated they were in for a moderate economic growth policy. It should be noted that Bulgaria can indeed count it as real success, if Budget 2006 only reallocates 40 per cent of the gross domestic product because, as it is, the budget re-allocates about 42 per cent,

and there is enormous pressure for further spending. The BSP's surge to deliver very fast on its political promises to raise income levels is the source of major concern. From the economic point of view, such an income raise would only be justified if it corresponds to the growth in labour productivity - which is obviously not the case in the budget-financed sphere. In parallel with higher salaries, there is also a process of further increasing the number of people on public administration payroll, thus further increasing the already excessive costs.

(2) The current situation of revenue collection by various institutions without uniform rules and a single information system is, on the one hand, a prerequisite for poor control and a good feeding ground for financial fraud, and, on the other, is a very expensive option due to the several-fold duplication of similar activities within different institutions and due to the higher administrative costs covered by payers. In order to improve the effectiveness and control on revenue collection, the establishment of a National Revenue Agency (NRA) was planned; the start of its operations has been delayed several times already and it is very possible that even the deadline of 1 January 2006 will not be met, as initially planned. The main reasons behind the NRA delay are related to the administrative incompetence of the previous government to draft and have approved by Parliament an acceptable draft of a Tax and Social Insurance Procedure Code (TIPC) and thus introduce uniform procedural norms on revenue collection. Another issue that was left unresolved by the previous government is failure to introduce a single information system in spite of the generous support given by the World Bank. Only after solving these two key issues can the new government proceed to launching NRA operations. The adoption of a Tax Insurance Procedure Code is expected in the near future; this is to be congratulated with the hope that it is legally viable and can be applied in practice.

(3) Economic actors find it important to know the direction in which Bulgarian tax policy is to develop as they base their business intentions, plans and estimates on such knowledge. What matters for them is not only the size of taxes (as is the case with most politicians) but also the economic logic behind the established tax rates. How can economic agents come to interpret the signals beamed by Bulgarian tax policy if it beams signals in all possible economic directions? In its report on fiscal transparency in Bulgaria, the International Monetary Fund also included its findings on the instability and difficult predictability of the tax system, which, on top of all else, treats taxpayers unequally.

A fine example would be the Socialists' promise of zero tax rates on reinvested profit. Although this proposal did not "make it" to the agenda of changes planned by the government, it will be again the subject of the discussions to follow. From the point of view of economy, it would be strange indeed to levy zero tax rate on profit tax if the dividend-tax continues to exist (removing dividend tax is not discussed by the coalition) because as it is there is a system of unequal treatment of reinvested and distributed profit. The former type is levied with a 15 per cent profit tax and the latter, with 15 per cent in profit-tax and 7 per cent of dividend-tax. The proposed zero rate for reinvested profit tax without the necessary changes in dividend tax results in the unjustified complications of company taxation, while Mr. Oresharski and his team declared they were in favour of simplifying the tax system. That is, either the dividend tax should be entirely removed, thus leaving only profit tax at a 0 per cent rate for re-invested and 15 per cent rate for distributed profit, or remove profit tax entirely and increase dividend tax to 15 per cent. It is very important for economic actors to be in the clear about policy-makers' intentions. For example as regards dividend policy investors will plan in advance and take measures to find legal loopholes to avoid dividend tax. The collection rate for this tax by end-August of 104.4 per cent speaks for itself that the seven percent rate is a poor incentive for tax avoidance, but with a range between 0 and 20.25 per cent, equal to the total burden of profit tax and dividend tax,, the motivation will be really strong.

From the economic point of view, the best solution would be to remove dividend tax and not introduce zero rates for reinvested profit tax. It is not efficient to have different tax rates for profit is reinvested in the same company and profit which is distributed in the form of dividend and could be more expediently invested elsewhere.

As part of the current discussion on taxes, all types of proposals are being made to policy-makers for present and future changes; a number of formal and informal talks are taking place. The main problem is however that the design of a tax system cannot be achieved through political negotiations; it is the fruit of an economically justified tax framework prepared by economic experts. This justified framework is however prominently absent both in the pre-election tax platforms of coalition partners and in the tax changes planned.

(4) In the field of financial decentralisation, BSP made an election promise of greater level of autonomy for municipalities in establishing the size of local taxes and charges. It is yet completely unclear how this is to be effected. Currently the procedure under which municipalities are financed is strictly centralized in spite of the Concept and Program for Fiscal Decentralisation. The changes planned under pressure from the International Monetary Fund to raise by about 20 per cent the tax base for real estate is a step towards increasing the revenues of municipalities from local tax and charges, but we should not disregard the fact that these measures will negatively impact the real property market and will have a strong anti-social effect. An increased tax base will result in raising real property tax and waste-collection charges to about BGN 220 m.

(5) A reduced tax burden is necessary to "unload" the taxpayers; as a result of this, they will be expected to contribute towards

accelerated economic growth. It is evident that a lower tax burden today is less feasible than it was around the middle or the end of the previous government's term of office. Today we have more reasons to be concerned that a considerable reduction of the tax burden would pose a threat to achieving another major economic goal of the new government: financial stability. If the tax burden reduction is in the area of direct tax, it will result in a more accelerated economic growth than if it is in the field of indirect taxation. Today this is much better understood by coalition partners than only a month earlier.

The Ministry of Finance proposals for changes are related precisely to transferring the tax and social insurance burden from direct tax to indirect tax, but the overall reduction of the burden is negligible or, even more possibly, non-existent.

A reduction of pension insurance contributions from 29 per cent to 23 per cent is proposed, which means alleviating the total social insurance burden from 42 per cent to 36 per cent. The contributions paid by employers and workers will be in a 65:35 ratio instead of the present ratio of 70:30 (employer/employee). This proposal corresponds to about BGN 600 m in the volume of collected social insurance contributions. Because the social insurance burden in Bulgaria is too high as compared to other countries the region, the decrease will reflect positively on Bulgaria's position in the rakings of foreign investment beneficiaries. Understandably, it must be borne in mind that the corporate tax rate is a factor of much larger significance to foreign investors' investment decisions than the rate of pension insurance. This reduction is required by the Bulgarian business community because the high pension payments are considered the reason for the inadequate numbers of new jobs and the thriving "shadow" economy.

An increase of the tax-exempt minimum is envisaged from the current BGN 130 to BGN 180 in 2006. This eliminates the 10 per cent rate and leaves unchanged the three brackets of respectively 20 per cent, 22 per cent and 24 per cent. This actual decrease in the taxation of lower income results in about BGN 220 m reduction in budget revenues.

In 2006 there are plans to increase the excise duty on cigarettes, alcohol and fuel, with the first two excise duties rising considerably. The Ministry of Finance plans an increase in excise duty revenues of BGN 390 m in total, which trails an increase in VAT revenues in the amount of BGN 78 m. Because "as a rule" excise duty collection is over-performed, these will be the minimum levels of excise duty and VAT increase. The actual figures will be 60-100 m higher.

(6) The International Monetary Fund report on fiscal transparency criticizes the establishment of the company "Public Investment Projects", which is extra-budgetary funded. The option that the Minister of Finance will be authorised to approve additional spending (provided revenues are over-executed and the budget balance is not compromised) is also not met with approval. This provision actually creates a legal base that would allow spending in excess of budget estimates. In addition, the Minister of Finance may re-channel one Ministry's budget credit to another Ministry within the same budget year. We share IMF's criticism and also insist that extra-budgetary spending should be stopped.

The areas in which, according to CED, Bulgaria should be improving its public finance policy are as follows:

- putting a stop to the practice of ever increasing budget surpluses and moving to a balanced budget;
- eliminating the options whereby the government can spend more than specified in the budget;
- limiting the level of budget reallocation to a maximum of the planned 40 % and gradually lowering that level by about 1 per cent per year;
- restructuring and upgrading the revenue collection system and in particular starting the operation of the National Revenue Agency (NRA);
- changing the philosophy of substantive law taxation system to less government intervention in the business decisions of economic agents;
- vigorous introduction of fiscal decentralisation;
- reduction of the overall tax and social insurance burden based on a justified economic concept;
- introducing family taxation.

The summer months of 2005 registered lower unemployment and a continuing increase of Bulgarians' real incomes. In the meantime, consumers show a growing pessimism about their future as compared to three months earlier. The labour market policy will continue looking for solution to tackle the high unemployment rate among people with low levels of education and long-term unemployed and the chronic shortage of highly qualified personnel. Under the influence of pre-election promises and riding on the momentum inherited from the past, the government declared its willingness to implement an income policy without however specifying in detail the purposes and methods of such policy. For the first time in Bulgaria the political will is in place to reduce the social insurance burden which is seen as a positive development both by the business community and trade unions, and by the expert community. The pension insurance market continues on its upward curve of development. It is in need of legislative support in the direction of developing the capital market and cooperation between businesses and pension insurance companies. The new team in the Ministry of Health demonstrates readiness to continue the health sector reform but, above all else, it needs a publicly coordinated political vision on the development of the Bulgarian healthcare model.

Labour Market

Employment and Unemployment. The summer months of 2005 improved the earlier record-low unemployment over previous years. The unemployment rate hit 10.77 per cent in August which is the lowest value for the past nine years. A positive development is that for six or seven months in a row now, the share of young people who found jobs has been growing. These purely quantitative developments hardly come as a surprise on the background of the registered economic growth, emigration, seasonal labour demand and subsidised employment programmes.

An issue still open for discussion however deals with the quality of jobs, that not only reduce the number of unemployed but also provide them with long-term and high-quality employment. In this situation, the intentions of the coalition government BSP – NMSII – MRF to create 240,000 new jobs and keep unemployment below 10 per cent for a period of four years sound acceptable and realistic; however, still to be proven in practice is the economic expediency of such a policy and the actual orientation to long-term employment at the expense of public communal activities in municipalities under the programme "From Social Benefits to Employment".

Labour Market Policy. In the course of the next several years the government will be faced with the difficult task of solving labour market problems related to the large number of long-term unemployed people (60.4 per cent of all unemployed) and the educational and professional discrepancies between labour force demand and supply. It seems that the current high unemployment rate is not so much the result of Bulgarian economy's incapacity to generate employment as the shortage of labour force having certain levels of education and professional training, and regional unemployment. The labour market policy should help overcome the regional gaps in employment and unemployment rates and create jobs for the poorly educated and long-term unemployed. For this purpose focusing more efforts on training and re-qualification is a must; in this way unemployed people with no education or professional training will be able to acquire professional skills for work in sectors and regions with the highest labour force deficit. As can be seen from several recent studies, the territorial mobility of the workforce is quite satisfactory and is not a barrier to labour resource movement provided that job seekers have the required knowledge and skills.

Employment and unemployment issues cannot be addressed without reforms in education. The now chronic shortage of highly qualified personnel requires improvements to the secondary and higher education systems.

These issues are of major importance to the current socio-economic development of Bulgaria, but, as is shown by the experience of new EU Member States from Central Europe and the Baltic region, the gaps are most severely felt only after accession. In these countries there is a concurrent labour force shortage and unemployment levels of about 8 per cent under the influence of foreign investments, moving production to the east, accelerated development in construction, tourism, and the services. The labour market policy in Bulgaria requires the simultaneous tackling of both problems, and, if possible, early preparation for this type of challenges. In parallel, the opportunities to deal with a similar situation are severely limited due to the deteriorated demographic situation and the unfavorable forecasts in this area.

Incomes and standard of living

The upward trend for real incomes persisted throughout the summer months of 2005. Although NSI data are somewhat outdated when published and we cannot trace the income dynamics at the time this report was drafted, obviously there is growth in incomes for the June-July 2005 period in the 4-5 per cent range as compared to the same period of last year. This conclusion applies to both wages as the major source of income and to total incomes according to the household budgets statistics.

Income and savings. The increase in real income during 2004 and 2005 means increased welfare level and better saving opportunities. In June 2005, savings were by about 30 per cent more as compared to the preceding year, mostly in the form of bank deposits worth about BGN 10.2 b There are grounds to forecast that incomes will continue to grow, as well as savings, not only in absolute terms but also in terms of income percentages. The short term of deposits however shows the relative insecurity as concerns future incomes.

A consumer survey in July of 2005 registered more pessimistic expectations related to changes in consumer prices in the course of the next 12 months. Households' perception of their financial condition is deteriorating, and pessimism for the future is growing. These conclusions come in conflict with forecasts made several months earlier but are probably the result of a more precarious general political and economic situation in the country and the increase in fuel and energy prices.

"Income Policy". Problems related to incomes and the standard of living were given special prominence after the new government started its term in office and the enhanced media activity of the social minister Emiliya Maslarova. She stated "active income policy" as her priority without however specifying in more detail the goals and methods of this policy. This proactive stand is in part explained by BSP's pre-election promises for a one-off increase of budget-financed salaries by 20 per cent and the Minister's political affiliation to this political force. Mrs Maslarova is very much convinced that this policy is necessary and possible now when Bulgaria's economy is mostly private and is developing in an environment of price and financial stability. Ambitions to conduct such a policy are probably based on inertia from past years when the state was the largest employer and Bulgaria lived through one inflation after another. Under those conditions, a policy in support of Bulgarians' purchasing power and establishing the size of minimum wages was both necessary and possible. This type of income policy must be left in the past. In this day and age, if we are to speak at all of government policy on income levels, then, with the entire convention of the name itself, we should limit efforts to monitoring and adjustment of minimum income while checking for their impact on the labour market and indirect intervention in support of businesses – building modern infrastructure and communications, an effective administrative system and a more favourable business environment.

The increase in budget-financed salaries and the minimum wage, the Christmas supplements to salaries and pensions etc. that were the subject of so many discussions over the past months should be reviewed very carefully and strictly aligned with the actual budget while taking into account the increase in labour productivity and keeping the financial stability.

Social Assistance

New Approach to poverty reduction. Even from her first public speeches, the Social Minister Mrs Emiliya Maslarova stated her intentions for a change in the welfare system and the implementation of a pilot project for supporting poor families in the form of social services in Stara Zagora municipality. This small attempt to diversify the range of social services by applying on a pilot basis options so far unfamiliar in Bulgaria deserves approval due to its innovative nature and the promising results from its implementation in other countries with high percentage of poor people who have little chance of improving their position because of the lack of job opportunities, education, and other factors. The project envisages that part of the social benefits will be paid as crèche or kindergarten fees for children of socially disadvantaged parents. Such programs ("social benefits on condition") have been implemented with success for years in Latin America and it is plausible to apply them in this country, too. The valuable thing about these programs is that it opens opportunities for children in poor families to get out of the poverty trap if they attend school regularly (that is, they abide by the "condition") and find a job afterwards.

The importance of these programs should not be overestimated and it is clear to all that enhanced economic development is the only way out of the poverty trap. But in view of forecasts for economic growth in Bulgaria in the course of the next 5-10 years, these programs have a logical place in the set of tools to fight poverty; moreover, the costs of such programs are not very high. In order for them to be efficient however, a strong and competent state administration is needed to channel the funds properly and monitor the results.

Social Partnership and Industrial Relationships

Dialogue with the business community and trade unions. After the government was formed, a series of meetings were held between ministers and representatives of trade unions and employers' organisation, including and meetings at the highest level. Apart from the official nature of the meetings, it should be noted that all three partners in the dialogue demonstrated their intentions for partnership and a constructive approach; these are of particular importance in view of the issues Bulgaria has to face, and the challenges before the coalition government. A positive development is that, through the social dialogue mechanisms, the subject of discussions are not only issues related to social policy, but a wider range of problems related to improving the business environment and the quality of human resources. The government should continue the positive tradition of active dialogue with the business community and trade unions - not only within the tripartite council but also with input from all key ministers whose responsibilities have to do with economic policy, administrative reform and improving the infrastructure.

Pension insurance

Major legislative changes and initiatives. The guidelines of tax and social insurance policy proposed by the Ministry of Finance (MF) in the course of the next year received support from the government in early October. For the first time in Bulgaria the political will is in place to reduce the social insurance burden which is seen as a positive development both by the business community and trade unions, and by the expert community. The relatively high social insurance burden in Bulgaria is indeed one of the barriers to improving the competitiveness of the Bulgarian economy, the employment rate and the standard of living of working people.

The option discussed for the insurance contribution to the Pensions Fund of State Social Security Insurance is to cut it down to 5 percentage points. According to MF estimates, a 5-6 points cut would leave in the hands of businesses about BGN 500-600 m which are expected to be invested in the modernisation of production, achieving compliance with EU standards and generating new jobs. The overall negative effect from reducing the insurance burden to be felt by the Pensions Fund budget at NSSI is estimated at about BGN 700 m. In the next year the state is expected to continue to finance its annual deficit by about BGN 600 m.

Unfavorable demographic trends, the relatively low level of employment, the enormous shadow sector of the economy and the expected decrease of the social insurance burden next year require innovative solutions that would guarantee the long-term financial stability of the social insurance budget. The idea promoted by the former government on establishing the so called "silver" fund with revenues from privatisation and license fees to support SSSI was a good innovative solution to this problem which should be translated into laws in the near future. Also needed is a speedier adoption of the new Tax Insurance Procedure Code so that the National Revenue Agency (NRA) could become fully operational next year and improve the effectiveness of tax and social insurance collection.

Over the past months, employers and trade unions succeeded in negotiating an eight percent average increase of the new minimum social insurance thresholds by commercial activities and groups of professions for 2006. This is in effect the largest increase of thresholds since they were first introduced in 2003 which is expected to partially compensate the loss of the Pensions Fund because of the planned cuts in social insurance rates; it however bears the possible risk of reduced competitiveness for some economic sectors. Branch associations and trade unions managed to reach an agreement on the minimum social insurance thresholds in 45 of a total of 70 commercial activities. As compared to last year, the number of reached agreements is down by five. The main reason for the smaller number of agreements is in the lack of a special Branch Associations Act which is expected to regulate which branch associations are legitimate and eligible to take part in annual negotiations. Some businesspeople continue to insist on the introduction of "seasonal" thresholds because of the seasonal nature of employment in some sectors.

Supplementary pension insurance. The positive trends in the pension insurance market development over the past years featuring an increase in the number of insured individuals and pension funds' assets continued also during the second quarter of the year. Nevertheless the supplementary pension insurance market is facing a number of internal and external challenges to which it will have to respond adequately if it is to continue on this upward trend.

Challenges internal to the system are related most of all to the need to better accommodate the needs of insured individuals. This could be achieved through developing and marketing pension products with various risk and profitability rates depending on the particular interest of insured individuals, as well as by seeking opportunities to more effectively manage the pension system funds and guaranteeing higher yield.

The system-external challenges are mostly related to Bulgaria's forthcoming EU membership and the need to coordinate the insurance models of separate Member States and develop strategies for pension insurance companies towards successful partnership with businesses in the real sector. In view of forthcoming EU membership, the country made a commitment to remove the privileged access of the state to the financial resources of pension funds. Therefore the limit for mandatory investment of pension assets in GS should be removed, and the allowances for other investment instruments should be increased. The special working group under the Agency for Economic Analyses and Forecasting, which also includes representatives of the Association of Supplementary Pension Insurance Companies and the Financial Supervision Commission, has already drafted amendments to the Social Security Code. What is now needed is for the Government to prove in practice that it supports the development of the supplementary pension insurance market - something widely declared in the political platforms of all coalition partners.

The CED forecast that assets in pension funds will exceed 1 b. BGN at the end of the year, now seems more than realistic. The potential of this major financial resource however is not yet fully geared towards improving the competitiveness of the Bulgarian economy, on the one hand, and ensuring better earnings of invested funds by insured individuals, on the other. To a large degree, the actions of pension insurance companies are restricted by the branch legislation and the lack of efficiently functioning capital market. Experts and key players on the pensions market expect the new government to keep its promises and take efficient measures to support the development of the pensions market.

Insured individuals. According to figures supplied by the "Social Insurance Supervision" Division at the Financial Supervision Commission (FSC) at the end of the second quarter of 2005, insured individuals in all supplementary pension insurance funds amount to over 2,843 million people, which means a 4.67 per cent growth as compared to the end of 2004, and 2.55 per cent as compared to the end of March this year. The largest increase in the number of insured individuals is observed for universal pension funds (UPF) – by 3.12 per cent over the end of the first quarter. The trend over the last few years on increasing the share of insured individuals in UPF (74.76 per cent), at the expense of the share of insured people at the other funds (OPF and VPF), still continues. Unlike the first quarter of this year when voluntary pension funds registered a slight decline in the number of insured individuals, during the second quarter a positive rate of increase of 1.09 per cent is observed, which could be partially explained by the relatively high yield of insurance funds.

Pension Assets. At the end of June, 2005. available net assets in pension funds are nearing BGN 940 m. which means a growth of 9.15 per cent as compared to the end of March and 19.27 per cent over the end of 2004. Once again, the highest growth in assets is reported for UPF, a fact explained by both the increased number of insured persons, the higher average income in the country, and the relatively good yield on the invested available funds. Another positive trend is that the rate of increase of pension funds is four times higher than the growth rate of insured individuals over 2004.

Investments. Figures on pension funds' investment activity reveal that they are still overly cautious and are not sufficiently active in looking at opportunities to more effectively manage insurance funds. Between 71 and 75 per cent of pension funds' assets continue to be invested in securities issued or guaranteed by the state, and in bank deposits. Another negative development is that the share of investment in shares and corporate bonds in investment portfolios of all three types of funds is going down during the second quarter of the year, which gives rise to skeptical expectations regarding the opportunities of Bulgarian business to make use of this available financial resource in the near future.

Voluntary pension funds continue to be conservative in their investment activity and do not make use of the recently established more liberal investment regime. Almost 50 per cent of their assets are still invested in securities issued or guaranteed by the state. The three groups of funds have invested respectively 12.58 per cent, 12.03 and 11.50 per cent of their assets in securities registered for trading on regulated markets.

The share of investment abroad as compared to overall investments is also growing at a negligibly small increment; this can be accounted for by both the inadequate investment position of pension funds and the insufficient yield provided by foreign securities. The new government's major efforts must be towards adopting measures for development of the Bulgarian capital market, promoting the cooperation between businesses and pension companies and establishing a predictable and effective investment and tax environment to further develop the pension insurance market.

Yield. The weighted average annual yield reported at the end of June from investment of UPF assets (10.52 per cent) and OPF (10.57 per cent) is greater than the mandatory minimum yield – by 6.31 per cent for UPF and 6.34 per cent for OPF, respectively. It is also higher than the inflation rate and the annual average interest rate on BGN deposits. Nevertheless the year-on-year yield at the end of March this year was higher than the yield on an annual basis reported at the end of June.

Concentration of the pension insurance market. The market concentration of the insurance market continues to be high. Three companies: PIC Doverie AD, PIC Saglasie AD and PIC Allianz Bulgaria AD continue to hold over 78 per cent of the net assets in the pension insurance system. These companies continue to provide services to over 75 per cent of all individuals insured in supplementary pension insurance funds. The pension market leader with the largest number of insured persons is still PIC Doverie AD, and the net assets leader is PIC Allianz Bulgaria AD. During the second quarter of the year, just like during the first, PIC Allianz Bulgaria AD, PIC DSK Rodina AD and "ING " AD were the best preferred companies by people who decided to transfer their accounts to UPF, OPF and VPF respectively.

This pension market configuration will continue as long as insured individuals are given objective incentives to transfer their accounts to a new pension fund. The identical structures of the investment portfolios of pension funds and lack of any discernible difference in investment yield so far beam no signals for a major shift of key players on the pension market in the near future. Experts in this field are more inclined to forecast a market consolidation than the emergence of new pension companies; this is usually explained by the relatively small scale of the market. Expectations are for new players to appear mostly as new majority owners or shareholders in existing companies because pension insurance is an increasingly attractive business. For the first half of the year 2005, five, instead of only four, companies, have shown positive financial results.

Table 4. Insured individuals in pension funds

	As of 31.12.04	As of 31.03.05	As of 30.06.05	Change 30.06.05/ 31.03.05, in %	Change 30.06.05/ 31.03.05, in %	Share of ins. individuals by funds as of 30.06.05
Number of insured individuals in supplementary PI funds	2716367	2772524	2843338	4.67	2.55	100.00
Number of insured individuals in UPFs	2004776	2061412	2125712	6.03	3.12	74.76
Number of insured individuals in OPFs	176175	177174	177884	0.97	0.40	6.26
Number of insured individuals in VPFs	535416	533938	539742	0.81	1.09	18.98

Source: FSC, "Social Insurance Supervision" Division, and own estimates

Table 5. Net assets available in pension funds

	As of 31.12.04	As of 31.03.05	As of 30.06.05	Change 30.06.05/ 31.12.04, in %	Change 30.06.05/ 31.03.05, in %	Share of pension insurance assets by funds as of 30.06.05
Net assets in supplementary PI funds , total, BGN thousand	787414	860420	939182	19.27	9.15	100.00
Net assets in UPF, BGN thousand	261125	299963	346825	32.82	15.62	36.93
Net assets available in OPF, BGN thousand.	200832	216056	228174	13.61	5.61	24.29
Net assets available in VPF, BGN thousand.	325457	344401	364183	11.90	5.74	38.78

Source: FSC, "Social Insurance Supervision" Division, and own estimates

Table 6. Market shares of PICs

Pension insurance companies (PICs)	Market share, in %									
	By number of insured persons in UPFs		By number of insured persons in OPFs		By number of insured persons in VPFs		By total number of insured persons		By net assets amount	
	As of 31.12.04	As of 30.06.05	As of 31.12.04	As of 30.06.05	As of 31.12.04	As of 30.06.05	As of 31.12.04	As of 30.06.05	As of 31.12.04	As of 30.06.05
PIC Doverie AD	42.10	40.73	40.71	40.30	27.26	27.48	39.09	**38.19**	33.18	**33.23**
PIC Saglasie AD	11.68	11.71	17.19	17.35	5.99	6.10	10.92	**11.00**	9.71	**9.75**
PIC DSK Rodina AD	7.32	7.66	4.36	4.69	4.63	4.07	6.60	**6.79**	5.25	**5.40**
PIC Allianz Bulgaria AD	20.06	20.57	21.29	20.98	47.84	48.11	25.61	**25.83**	35.51	**35.07**
"ING PIC" AD	9.49	9.50	5.66	5.69	4.67	4.75	8.29	**8.36**	7.62	**7.81**
PIC CCB-Sila	4.31	4.41	3.95	4.05	3.18	3.22	4.06	**4.16**	2.06	**2.10**
PIC LUKoil Garant Bulgaria AD	3.77	3.79	5.98	5.86	5.89	5.65	4.33	**4.27**	6.29	**6.05**
DZI Pension insurance AD	1.27	1.62	0.86	1.08	0.54	0.63	1.10	**1.40**	0.38	**0.59**
Total	100.00	100.00	100.00	100.00	100.00	100.00	100.00	**100.00**	100.00	**100.00**

Source: FSC, "Social Insurance Supervision" Division, and own estimates

Table 7. Investments of pension funds in various financial instruments

Investment Types	Total for UPF		Total for OPF		Total for VPF	
	As of 31.03.05	As of 30.06.05	As of 31.03.05	As of 30.06.05	As of 31.03.05	As of 30.06.05
1. State-issued or state-guaranteed securities	54.60	54.45	56.20	57.52	50.88	49.29
2. Securities registered for trading on regulated markets	13.34	12.58	12.43	12.03	11.69	11.50
2.1. Shares	5.40	4.97	4.75	4.65	3.96	3.93
2.2. Corporate bonds	7.95	7.61	7.68	7.38	7.73	7.57
3. Municipal bonds	0.84	1.01	0.87	1.04	0.40	0.51
4. Bank deposits	19.03	20.94	19.60	18.81	20.87	22.49
5. Mortgage bonds	10.99	9.70	9.07	8.66	12.78	11.88
6. Investment Property	0.41	0.62	1.45	1.54	2.70	3.61
7. Investment abroad	0.79	0.71	0.38	0.40	0.68	0.72
8. Derivates	0.00	0.00	0.00	0.00	0.00	0.00
Investments, total:	100.00	100.00	100.00	100.00	100.00	100.00

Source: FSC, Social Insurance Supervision Division

Table 8. Insured individuals and funds transferred by PIC

Pension insurance companies (PIC)	UPF				OPF				VPF			
	Number of insured individuals (01.01.05-30.06.05)	Funds (BGN)	Number of insured individuals (01.04.05-30.06.05)	Funds (BGN)	Number of insured individuals (01.01.05-30.06.05)	Funds (BGN)	Number of insured individuals (01.04.05-30.06.05)	Funds (BGN)	Number of insured individuals (01.01.05-30.06.05)	Funds (BGN)	Number of insured individuals (01.04.05-30.06.05)	Funds (BGN)
PIC Doverie AD	-7903	-1,480,157	-5073	-1,015,643	-212	-357231	-266	-577,930	-116	196337	-39	74556
PIC Saglasie AD	-3434	-611710	-2327	-407875	-118	-197253	-184	-194047	-187	-116276	-166	-56811
PIC DSK Rodina AD	4131	769197	2493	470989	299	503674	205	323087	-187	-285458	-179	-253544
PIC Allianz Bulgaria AD	7612	859411	5484	651802	-168	-712097	88	-101022	7	-329769	64	-186652
“ING PIC” AD	-2794	-143790	-2173	-139452	172	532811	113	330363	359	550009	238	395304
PIC CCB-Sila	-700	41763	-414	58404	-77	4264	-27	74343	-129	-177890	-62	-46636
PIC LUKoil Garant Bulgaria AD	126	58001	46	35270	-14	82211	4	70000	61	2028	31	12434
DZI Pension insurance AD	2962	507285	1964	346505	118	143621	67	75206	192	161019	113	61349

Source: FSC, Social Insurance Supervision Division

Healthcare Reform

The new team in the Ministry of Health demonstrates readiness to continue the health sector reform but, above all else, it needs a publicly coordinated political vision on the development of the Bulgarian healthcare model. Pre-election political programs revealed a relatively good level of understanding of the problems faced by the healthcare system, but the proposed solutions were not associated with a system of key actors' rights and responsibilities clearly distributed over time.

The for top policy priorities for the new MH team:

- improving the status of Bulgarian citizens and putting the patient at the center of healthcare reform;
- overcoming the demographic crisis through special programs for child, mother and school-based healthcare;
- improving the financial stability and the economic effectiveness of the healthcare system, and
- accelerated implementation of MH commitments related to European integration and expanding international cooperation.

A major challenge to the financial stability and the economic effectiveness of the healthcare system is linked to the poor funding mechanism for in-patient healthcare establishments which disrupts Bulgaria's healthcare reform. Because of the insufficient funding of the health system as a whole due to the diluted responsibilities of the two sources of funding (Health Insurance Fund and the Ministry of Health) and the unrealistic pricing of medical activities, the new Health Minister believes that hospitals continue to accumulate debts to their suppliers mostly because of specific medical and financial management of individual hospitals. This is also the reason for the inspections in state hospitals ordered by the Minister; these hospitals traditionally account for about 70 per cent of all debt in the healthcare system.

The price increase for about 50 NHIF-reimbursed medicines for patients starting this year also made the new minister request a special enquiry into the prices of medicines in Hungary, Poland, Czech Republic and Bulgaria. The goal is to analyze how many of these medicines are sold at higher prices in Bulgaria and then take measures to cut their prices. According to experts, the primary reason behind the price increase for medicines is related to introducing VAT and the way NHIF pays to drug manufacturers. The health fund has the right to include in its list drugs at prices that are higher than in other countries but cannot pay to pharmaceutical companies more than the average European price of the drug.

In order to avoid a situation where the health system is underfinanced in 2006 the accumulated debt cannot be covered, the Health Minister will propose an increase of health funds under Budget 2006 to 5 per cent of GDP. Although the Health Fund and the Bulgarian Medical Association insist on raising the health insurance contribution as early as 2006, for the time being there are no indications of political decisions in this direction. The overall conclusion is that, without changes in the way healthcare is financed and without a more rational use of the limited funds, hospitals will continue to accumulate debt in the course of next year. The absence of a uniform information system in healthcare creates negative expectations regarding its preparedness to introduce the so called diagnostically related groups in 2006, this approach is expected to achieve a more realistic pricing of medical activities.

The government is discussing an option under which, starting from 2006, the Health Insurance Fund will not pay the entire price of treatment of insured individuals at hospitals but part of the health service costs will be covered by patients themselves and another portion will be financed by private health insurance companies. The future financial scheme in healthcare will depend, above all, on the political will of coalition partners, and the capacity of the national budget.

In CED's opinion, key priorities in social policy must be on:

- improving the quality of new jobs so that they guarantee long-term employment and career development to formerly unemployed people;
- orientation towards long-term employment at the expense of public communal activities in municipalities under the programme "From Social Benefits to Employment";
- achieving a balance between demand and supply on the labour market through targeted educational policy;
- transition from a welfare policy of erratic spending towards an income policy based on economic effectiveness.

In order to secure the long-term financial stability of the SSSI, the government should:

- support the creation of the so called "Silver Fund";
- undertake the necessary legislative measures to ensure the actual operations of the National Revenue Agency;
- support the adoption of the Branch Associations Act, and
- take additional measures to upgrade the negotiation mechanism between trade unions and employers on establishing the annual minimum social insurance thresholds, expected to be increased by an average of 8 per cent next year .

Major challenges in healthcare to which the new coalition government must respond with adequate measures, are related to the need for:

- a change in the mechanism in-patient healthcare establishments are funded;

- reducing the basic services package covered by the Health Insurance Fund;
- taking efficient measures to develop private health funds;
- conducting effective privatisation of healthcare establishments;
- building a comprehensive information system in the sector;
- solving the issue of uninsured individuals, and
- ensuring transparency in tenders for expensive medicines.

During the review period, legislative work in the area covered environmental noise management, waste and packaging waste management, sustainable use of soils, and packaging waste, major industrial pollution and major accident prevention. The procedure for participation of Bulgarian companies in the European scheme for greenhouse gas emission allowance trading was launched.

In September, the National Assembly adopted the **Environmental Noise Protection Act** (OG, No 74 of 13 September, 2005.). The new law transposes Directive 2002/49/EC relating to the assessment and management of environmental noise, and will come into force on 1 January, 2006 – one year later than the deadline negotiated under the Environment Chapter.

With the new Act public administration will be obligated to monitor the level of noise emissions from automobile traffic, railways, airplanes and large industrial enterprises. The scope of this law will cover categories of noise emitted at work places, noise from domestic activities, due to military activities and other specific sources.

Strategic Noise Maps

A major tool in environmental noise control and management introduced with the new law is the drawing-up of Strategic Noise Maps.

Noise maps will be prepared in Bulgaria for the first time and will contain information on over-the-limit noise pollution in a given region, dwellings, the number of people living in them, childcare and health facilities, schools and research organisations exposed to noise emissions above the set limits. Regions of excess noise levels having adverse impact on human health will be identified. After analyzing the situation for the preceding year and preparing a forecast for the anticipated noise situation, the information reflected in noise maps will be used for drawing up specific Action Plans.

Strategic maps will be prepared by the mayors of municipalities, as concerns human settlements. The Minister of Transport or a person authorised by the Minister will be responsible for preparing Strategic Noise Maps for major railway lines in the country, and the Minister of Regional Development and Public Works will be responsible for major roads of national significance. Noise maps will be reviewed each 5 years and must be accompanied by a noise forecast for the region and an action plan for noise control. For human settlements with over 250 thousand residents, for major roads with over 6 million vehicle passages per year, for railways having over 60 thousand train passages per year, and for airports, the deadline for preparing noise maps will be 30 June, 2007. For other agglomerations, major roads and railways, the deadline will be 30 June, 2012.

Noise maps are a major component in the provisions of Directive 2002/49/EC. They are the basis of comparison of environmental noise information at national and local level in Member States and also a baseline for noise pollution, risks to human health and measures adopted in this area. The first maps it Member States are expected in 2007 and the first Action Plan will be ready in 2008. The Directive requirements will serve as basis for developing follow-up measures by the European Union on reducing environmental noise emitted by major sources of pollution identified at an earlier stage. In 2009, the European Commission is bound to present to the European Parliament a common report on the implementation of Directive 2002/49/EC and proposals for policy changes and future Community action vis-à-vis environmental noise.

Environmental Noise Information

The newly adopted law defines environmental noise information as public information and creates an obligation for authorities to inform the public and the European Commission on any new noise pollution and forecasts for possible cases of exceeded emission limit values. A specific procedure is established for public access to approved strategic noise maps for regions and to approved action plans, including by means of modern information technologies. Institutions having their own websites will be obliged to publish any available information on noise pollution in electronic form.

Competencies of government bodies and local government structures, of legal entities and sole-proprietor merchants

The Environmental Noise Protection Act provides for measures aiming to increase both the responsibilities and the competences of local authorities. Control on human health protection against the harmful impact of noise caused by local sources will be exercised by the Minister of Health or specially authorised officials through the National System for Urban Noise Monitoring and Assessment of Harmful Effects of Noise on Human Health.

The Minister of Environment and Water and the Directors of Regional Inspectorates of Environment and Water or officials authorised by them will exercise control on installations and facilities in industry. For categories of industrial activities under Annex No 4 to Art. 117, Para. 1 of the Environmental Protection Act (EPA) the requirements under the Environmental Noise Protection Act will be satisfied with the procedures issuing an integrated permit.

Owners of industrial installations which represent noise sources will have to reports on noise levels before regional inspectorates of environment and water.

Sanctions for violating the limit values for individuals amount to BGN 500 to 1, 000, and for legal persons and sole-proprietor merchants – from BGN 1, 000 to 3, 000.

Environmental noise indicators at various times of the day or night, limit values for environmental noise indicators, the methods of assessment of noise indicators and the methods for assessment of the harmful effects of noise on human health are not specifically defined in the newly adopted law. These will be established in dedicated Ordinances by the Minister of Health and the Minister the Environment and Water.

The Noise Act was a long-awaited and important stage of the full transposition of the environmental *acquis* and the European Union common policy on environment. Prior to the adoption of the new law, the numerous ordinances governing this area set the ground for doubling and "diluting" the competences of government institutions and thus resulted in the insufficient protection of people from the harmful impact of noise. The overall assessment of legislators is that, within national law, for the first time a major step was taken towards the comprehensive regulation of this subject matter being closely related to improving the quality of people's living environment, particularly in urbanised areas.

However the Environmental Noise Protection Act was adopted without covering some key elements of Directive 2002/49/EC, such as harmonized noise indicators and limit values for noise emissions for major noise categories. Because of this, at this stage it is not possible to assess the effectiveness and potential impact of legal texts and procedures. It is unclear to what degree the act will impact the quality of infrastructure, the urban environment and, more generally, people's health and living conditions. Its most significant impact is expected to be increasing the competences of local authorities and government institutions in the collection and storage of comparative information regarding the sources of noise pollution and improving its quality for planning and reporting purposes.

The Environmental Protection Act was amended and supplements by the National Assembly on 14 September 2005 (Act on Amendments to EPA, Official Gazette, No 77 of 27 September, 2005). The amendments affect several categories of activities and are related to improving the quality of environmental information and regulating public access to such information.

All legal entities and individuals involved in activities and services related to the environment are obliged to provide information on the state of environmental components. Authorities at the national and local level are obliged to provide any available information on the environment, and the authorities maintaining webpages will be obliged to provide and update a publicly accessible database including the texts of policy papers, programmes, progress reports on the legislative implementation, environment monitoring data, public registers, EIA decisions, registration, licensing etc.

The regional environmental inspectorates will be obliged to prepare annual regional reports on environmental indicators for the respective area containing data for the preceding year which will be publicly accessible and will be included in the National Report.

Requirements to Sustainable Use and Recovery of Soil

Defining soil as a limited, irreplaceable and practically irrecoverable natural resource, amendments to EPA prescribe the application of good practices in soil use. The law lists specific obligations of legal entities and individuals who own or use landed property for preserving the quality, recovery and elimination of harmful soil modifications as a result of damage, pollution and soil degradation. The damaged areas will be subject to inventorying and, following an assessment of the degree and nature of modifications, recovery measures will be prescribed.

Major Accident Prevention

Pursuant to EPA amendments, operators of installations at which hazardous substances are being stored or used, shall be obliged to classify the installation as a plant/installation of low or high risk potential. New enterprises or installations with risk potential will be constructed only after having been issued with a permit and having prepared individual major incident prevention programmes and plans for measures ensuring a high level of protection for the population and the environment. Operation of existing facilities classified as low or high risk potential will only be possible following the issue of a permit by the Minister of Environment and Water. The issue of the permit involves publishing all documents associated with the procedure on the MoEW website and one-month public access to these documents. Operators of installations with high risk potential will be obliged to submit safety measures and emergency action plans.

Risk classification is not required for military enterprises, hazards related to ionizing radiation, transportation of hazardous substances outside enterprises, prospecting and extraction of mineral resources, including oil and gas in the coastal area as well as landfills with the exception of those containing hazardous substances.

The classification criteria for a new or existing enterprise and/or installation where hazardous substances are used and/or stored, are specified in a special Annex to the Act.

Greenhouse gas emission allowance trading scheme

Pursuant to the amended EPA, the emissions trading scheme is open to natural person and legal entities in Bulgaria, the

European Union and countries with which Bulgaria has signed agreements. The law contains a regulated procedure on the drafting of a **National Allocation Plan for Greenhouse Gas Emission Allowances.** The Plan aims to establish the total quantity of allowances, its distribution among operators of installations, the list of installations and the quantity of allowances for each installation. The first National Allocation Plan will cover the period January – December, 2007

MoEW will maintain and update a National Register to report the granting, possession, transfer and revocation of greenhouse gas emission allowances. Operators of installations will provide the competent authority on issuing and revocation of allowances (the Minister of Environment and Water) annually with the established number of allowances, equal to the quantity of emissions by the respective installation. For each tonne of carbon dioxide equivalent for which the operator did not submit allowances, the penalty payment is in the amount of BGN 200 per tonne of CDE; from 1 January 2007 to 1 January 2008 the sanction will be BGN 80.

Only allowances issued by the competent authority of an EU Member State will be eligible, and also emission reduction units issued in compliance with the UN Convention on Climate Change. Emission reduction units and certified emission reduction units will be used in the emission allowances trade starting from 1 January 2008.

MoEW started the procedure to identify enterprises eligible for participation in the EU emissions trading scheme. It includes not only existing installations but also installations expected to start operating which will fall within the scope of Directive 2003/87/EC. The Ministry of the Environment and Water webpage contains a list of categories of activities falling within the scope of the Directive and Bulgarian legislation.

Amendments to the Waste Management Act

With the amendments introduced in EPA, some changes were also applied to the Waste Management Act. The activities of collection, transportation, temporary storage, disposal and/or recycling of waste can be performed by both Bulgarian and foreign legal entities and individuals.

The size of sanctions and the scope of individuals subject to punitive sanctions for law violations have been increased. For any violations of this Act, individuals, mayors of municipalities and authorised officials will be sanctioned with a penalty payment of BGN 1,000 to 10 thousand; for legal entities and sole-proprietor merchants the sanction is between BGN 1,000 and 20 thousand. A repeated offence is sanctioned with a double penalty payment.

The property sanction will be applicable to sole-proprietor merchants or legal entities who failed to carry out waste classification or who place on the market packaging without designating the materials used to produce such packaging or sell packaging containing heavy metals.

Packaging waste recycling commitments

By 2011 the recycling waste target set by the law is a minimum of 60 per cent of the weight of packaging waste to be recycled or incinerated at waste-incineration plants installations with energy recovery. Amendments to the Waste Management Act also introduce changes to the recycling targets for packaging waste which are increased: from 45 per cent to min. 55 and max. 80 per cent of the weight of packaging. The hardest requirements are set for the recycling of glass, paper and board packaging. Higher requirements are set also as regards the percentage of packaging waste subject to recycling; targets must be met in the 2006-2010 period, and especially for the years 2006, 2007 and 2008.

Amendments to the WMA and the new deadlines for meeting targets gave rise to some reasonable concerns about the adopted pattern of meeting EU commitments in this are regarding the actual condition of the waste issue and the impact it has on companies and citizens.

Requirements in the previous version of the law were set at a minimum of 20 per cent packaging waste recovery (for 2004) and at least 25 per cent for 2005. For this purpose, the necessary settings were put in place for private operators and municipalities to use licensed companies or the Enterprise for Management of Environment Protection under the MoEW when they are not capable of applying waste recycling or recovery activities.

The official results of work accomplished in 2004 will be announced on 30 November 2005, the publishing date of the report by the Executive Agency on the Environment and Water. As of today, MoEW data reveal that, in total, packaging waste recovery organisations 665 (companies) and those organisations that individually meet their obligations (a of total 23 companies) have placed on the market 150,446 tonnes of packaging of which 33,528 were recycled, which accounts for 22.29 per cent.

Based on these figures and with estimates for 347,000 tonnes of generated packaging specified in the Programme for Implementation of Directive 94/62/EC on packaging and packaging waste, MEW reports that packaging waste recovery organisations have covered about 34.21 per cent of the total quantity of packaged goods on the market, and those individually meeting their obligations have covered 9.66 per cent, i.e. a of total 43.87 per cent, thus achieving a total percentage of recovery of 22.21 per cent for 2004.

With this optimistic assessment of results achieved under the current waste recovery model and the insufficient rate of building new household waste facilities, it is not clear on the basis of what estimates and with what additional resources the higher recovery targets will be met as specified in the latest amendments to the law; it is also yet to be seen whether the amendments were not in themselves the response of government institutions to the increasingly alarming situation in this sector.

Financial sector and financial mediation in Bulgaria are still dominated by the banking system. The statistics from the last quarter show that the taming of the credit expansion, as expected, had been a temporary phenomenon. The credit expansion has restored its previous pace, and our concerns with regard to the mid and long-term stability of the banking system are again revived. We continue to insist on the termination of the administrative measures in view of their inefficiency and on adopting more market-oriented measures.

Bank and monetary statistics[24]

Money supply. Data for the money supply can be received from two different sources of BNB: (1) the press release and (2) the weekly monetary statistics. With regard to money supply, there is some disparity between the two sources, so we try to reflect these differences.

According to the press release of BNB, broad money[25] increases by BGN 434 million compared to the previous month and reach BGN 23.2 billion, representing 56 per cent of GDP with projected amount for 2005 of BGN 41.4 billion. At the same time according to the weekly monetary statistics of BNB, broad money at the end of June is BGN 22.843 billion while at the end of July - BGN 23.219 billion which represents a growth of BGN 376 million. As per the press release of BNB, the growth in money supply[26] is 1.9 per cent, which is near the average percentage (2.0 per cent) for the last 12 months, while as per the monetary statistics, the rate of growth of money supply is 1.6 per cent.

The growth of broad money for August is 1.7 per cent compared to the previous month. The annual growth of broad money M3 for August towards previous August is 28.3 per cent.

Quasi-money[27] marks a decelerating trend – 1.1 per cent at an annual average rate of 1.7 per cent. On the other hand, the low liquid elements of money supply mark a fall of BGN 16.6 million.

Monetary resources: net foreign assets. After a quarterly increase, net foreign assets mark a decrease by BGN 394 million (3 per cent), Foreign assets decrease by BGN 965 million while the liabilities by BGN 571 million and the difference between the assets and the liabilities (965 – 571 = 394) corresponds to the change in the net foreign assets. Both changes are explained mainly by the buyback of the Brady bonds: the decrease of assets (965) is related to a great extent to the decrease of the foreign assets in the Central Bank as a result of payments while the decrease of liabilities is a result of the decrease of the foreign indebtedness.

Monetary resources: net domestic assets. Domestic credit increases by BGN 895 million, while net domestic credit increases by BGN 855 million. On the other part, net domestic credit is divided into government and non-government. The net government credit (claims on general government sector) increases by BGN 632 million while the non-government sector by BGN 263 million (632 + 263 = 855).
The increase of the net government receivables is a result of the decrease of the fiscal reserve by BGN 615 million that was used for repayment of the Brady bonds, and to the additional increase of the domestic BGN debt for July by BGN 77 million.

The specific data behind those figures are as follows: As per the data of the Ministry of Finance, the fiscal reserve at the end of July totals BGN 4661.5 million while at the end of June it is BGN 5276.9M, which is reflected as a decrease of the net indebtedness to the government by BGN 615.4 million = BGN 5276.9 million – BGN 4661.5 million. Based on the data of the Ministry of Finance for the national debt, the domestic debt at the end of July totals EUR 1 456 while at the end of June it is EUR 1417 which marks an increase of the internal indebtedness for July by EUR 39 million or approximately by BGN 77 million. In other words, the increase of the net government receivables by BGN 632 million is reflected in the decrease of the liabilities of the government by BGN 615 million and in the additional government credit of BGN 77 million, which are partially compensated by over-fulfillment of the July budget.

Money multiplier[28]**.** There is some lack of correspondence between the official press release and the weekly monetary statistics published by BNB. According to the press release the monetary base in July has increased by BGN 35 million, reaching BGN 7 322 billion. The statistics report an increase from BGN 7 055 billion for June to BGN 7 322 billion for July, which makes an increase by BGN 267 million. The money multiplier in the press release *grows* up to 3.17 while the statistics show a drop of the money multiplier to 3.17 for July compared to 3.24 for June. The main discrepancy appears in bank reserves – the press release shows a drop of the reserves by BGN 175 million while the statistics show an increase from BGN 2183 million to BGN 2265 million, a growth of BGN 82 million.

Assets. At the end of July, total assets of the banking system reach BGN 28 118 573 thousand. For a period of one year the balance sheet figure of the banking system grows by +36.2 per cent (BGN 466 751 thousand) while compared to June the growth is +0.7 per cent (BGN 92 053 thousand). The increase compared to the previous month is a result of the growth of the net loans to non-financial institutions (NFI), increase of

24 As per the official press releases and the official monetary statistics of BNB, www.bnb.bg.

25 Broad money, a measure for money supply, include currency outside banks, overnight deposits, quasi-money, repo agreements and issued debt securities with a term of up to two years.

26 Money supply is measured by broad money. See previous note.

27 Quasi-money apart from reserve money includes deposits with agreed maturity of up to 2 years and deposits redeemable at notice of up to three months.

28 The monetary multiplier represents the ratio between the money supply (broad money) and the monetary base (reserve money). For example, broad money for August is BGN 23.6 billion, the reserve money is BGN 7 billion and the money multiplier is 23.6/7.6=3.1 A.

the claims on financial institutions as well as of the investment portfolio.

The increase in these balance sheet aggregates totally compensates the shrinkage of cash and the investment portfolio. As of July, the banks in Group I hold 74.2 per cent of the assets of the banking system; the credit institutions in Group II hold 20.7 per cent and those in Group III 5.1 per cent. A slight increase of the share of the small and medium size banks is being observed.

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Deposits. The growth of the assets of the banking system is funded by the growth of the deposits from non-financial institutions and other customers, which grew by BGN 419 746 thousand (+2.3 per cent) by the end of July compared to the end of June. The upward trend of deposits from corporates and households during this month compensates the downward trend of deposits from financial institutions, which decrease by BGN 161 913 thousand or by – 4.3 per cent. In July, term deposits of

NFI increase by BGN 588 970 thousand (+7.0 per cent), while the total amount of demand deposits shrinks by BGN 181 135 thousand (-2.5 per cent). At the end of July, the total deposit base of the banking system amounts to BGN 22 027 340 thousand and within a year horizon it increases by +38.3 per cent (BGN 6 099 016 thousand). Compared to the previous month the growth is +1.2 per cent (BGN 257 833 thousand) and the largest variation is observed in the BGN deposits (growth by BGN 300 093 thousand). The market share of the total deposit base in the banking system is respectively 75.2 per cent for the banks in Group I, 18.9 per cent for the banks in Group II and 5.9 per cent for Group III. For the last twelve months the deposits from financial institutions increase by BGN 1 416 614 thousand (+64.2 per cent) while deposits from non-financial institutions – by BGN 4 682 402 thousand (+34.1 per cent).

Foreign currency deposits reach BGN 8.2 billion (20 per cent of GDP), thus marking a 2 per cent growth at an average monthly growth rate for the year of 1.3 per cent. For the last twelve months, the share of the foreign currency deposits has fallen by 4.3 per cent reaching 45.4 per cent of the total deposits within M3. These figures could be interpreted from an economic point of view in two ways: (1) the demand for BGN increases and (2) the general economic trust in BGN as currency increases.

Funding resources. The total amount of all funding resources (deposits, long-term and short-term loans) is BGN 23 927 720 thousand and compared to June they increase by BGN 286 728 thousand (+1.2 per cent).

Credits. At the end of July the net loans to non-financial institutions reach BGN 15 870 786 thousand and remain the most important balance sheet asset representing 56.5 per cent of all the assets. Within a year the net loan portfolio grows by BGN 4 452 720 thousand (+39 per cent) and mortgage loans report their largest growth (+140.5 per cent). The only decrease for the same period is under the item “Other loans” (-35.3%). The net loan portfolio increases by BGN 258 572 thousand (1.7 per cent) compared to June and in terms of type of currency the largest increase is in BGN (BGN 183 425 thousand) followed by EUR (BGN 99 996 thousand) while the rest of the foreign currencies decrease by BGN 24 822 thousand.

Consumer loans mark the largest variation in absolute terms (BGN 110 350 thousand). It should be pointed out that the annual growth of these loans is +55.8 per cent while the monthly growth is +3.1 per cent. The mortgage loans mark a monthly growth by BGN 84 574 thousand (+5.6 per cent) while commercial loans, dominating the loan portfolio, increase by BGN 67 177 thousand (+0.6 per cent). The market share of the banks in Group I in terms of the total loan portfolio to non-financial institutions is 74.5 per cent; the banks in Group II hold 19.5 per cent and the banks in Group III 6.0 per cent respectively.

Maturity structure of non-government credits. In July, loans with maturity over 1 year and up to 5 years have the largest relative share of 43.3 per cent, followed by loans over 5 years – 33.7 per cent. The overdrafts and the short-term loans (up to 1 year) represent 14.3 per cent and 8.7 per cent respectively. Compared to the previous year, the share of long-term loans has increased by 8.2 per cent, which is mainly at the expense of loans with maturity 1 to 5 years. In other words, the loan maturity in the banking system has lengthened.

Currency structure of non-government credits. Loans in BGN represent 52.5 per cent, in EUR 42.5 per cent and in other currencies only 5 per cent. Compared to previous years, the share of loans in EUR increase by 4.1 per cent mostly at the expense of loans in other foreign currencies, which decrease by 3 per cent. The corporate loans are dominated by Euro loans – 60 per cent while in loans to households BGN loans are 87 per cent.

Credit substitutes and other off-balance sheet commitments increase by BGN 234 931 thousand (+5.0 per cent) compared to June and within an year horizon they mark a growth of BGN 1 809 791 thousand (+57.7 per cent).

Banking system equity, per balance sheet data, reaches BGN 3 091 941 thousand and the positive variation of BGN 58 986 thousand (+1.9 per cent) compared to the previous month is a result of the banks` current increase in profits. For one year the total equity of banks increased by BGN 598 789 thousand (+24 per cent).

Profit. The profits reported by the banking system at the end of July 2005 amount to BGN 337 959 thousand. Compared to the same period last year the financial result increases by BGN

80 239 thousand (31.1 per cent). At 31st of July 2005 the Group I banks generate 81.7 per cent of the banking system profit, Group II banks generate 14.0 per cent and the credit institutions in Group III – 4.3 per cent of the net financial result.

Table 9. Main indicators of the banking sector per bank groups

	Group I	Group II	Group III
Assets	74.2 per cent	20.7 per cent	5.1 per cent
Deposits	75.2 per cent	18.9 per cent	5.9 per cent
Loans	74.5 per cent	19.5 per cent	6.0 per cent
Profit	81.7 per cent	14.0 per cent	4.3 per cent

Source: BNB

The table above summarizes the main indicators (assets, deposits, loans, profit) per bank groups. It should be mentioned that the small banks (Group II) use 19.5 per cent of the deposits in the sector in order to generate only 14 per cent of the sector profit.

Irrespective of whether we juxtapose the profit to assets, deposits, or loans, the conclusion is that the small banks are comparatively inefficient compared to the big banks. In order to clarify whether the reason for this is in the lower profitability of assets, in the higher price of capital or in their bigger general/operative expenses, a detailed analysis should be done. In any case, the relative inefficiency of the small banks means that prerequisites exist for additional consolidation of the banking sector by acquisition of the relatively inefficient small banks from the large ones. This gives us grounds to expect continuation in the consolidation process of the banking sector in the short and mid-run.

Credit and monetary expansion.

Irrespective of the BNB regulations, the inflationary pressure in the economy continues to grow. Our previous publication reflected the temporary success of the last regulations of BNB in their attempt to calm down the credit expansion. We made the qualification that such administrative measures have a short-term effect, after which the expansion restores its aggressive trend. That was the speculation we expressed then; currently we have enough data for analysis.

First, the statistics show that the credit expansion was halted only for two months. The end of April marks a control of the expansion with a total amount of the domestic credit of BGN 16 billion. This control coincides with the last modification of the regulation dated 21st of April. At the end of May and June the domestic credit dropped down to BGN 15.7 billion and BGN 15.5 billion respectively.

Second, since July the credit expansion restored its previous pace. At the end of July, the domestic credit is BGN 16.2 billion, at the end of August it is BGN 16.5 billion and in the middle of September (the end of second week of September) it is BGN 16.7 billion. This represents a growth of 8 per cent (7.978 per cent) for a period of two months and a half, which on annual basis equates to a growth of 45 per cent. (Calculated by raising 1.08 to the 12/2.5th degree, which gives exactly 44.7 per cent). Although a period of 2.5 months is admittedly a relatively short term period for serious conclusions, it shows that the credit expansion has almost restored its aggressive pace of 49-50 per cent annually prior to the regulation, while the current pace is 45 per cent.

With the regulation, BNB aimed at a growth of 30-35 per cent though giving no explicit argument for that growth in public. On our part, CED calculated, on the basis of the macroeconomic savings, that the optimum growth of loans for 2005 is around 30 per cent, which well correspondents to the aims set by BNB. The growth of 45 per cent realized during the last two and a half months should be interpreted as too excessive in the light of the aimed growth of 30-35 per cent and the regulation of BNB as unsuccessful.

Third, it is important to point out that it is tempting to calculate the growth of the credit expansion including the months of May and June. Such calculations give considerably smaller and more acceptable credit growth and the BNB regulation seems more successful. This type of calculation, however, is methodologically incorrect and tricky, as it creates the illusion of the effectiveness of the regulation and gives possibility for manipulation of the statistics by randomly choosing the initial and the final period for calculations. Actually, the initial period should not be chosen at random, but in accordance with the depletion of the short-term effect of the regulation and from the commencement of the expansion restoration, i.e. beginning of July in this particular case.

Fourth, the lack of efficiency of the regulation is confirmed by the growth of money supply (broad money), which continues to grow aggressively and unrestrained by the BNB regulations. Table 10 illustrates the assertion above.

As the table shows, the money supply in May, June and July grows by +2.1 per cent, +1.6 per cent and + 1.6 per cent. Actually, for the last 12 months (from August to August), money supply has increased by 28.3 per cent, i.e. 2.1 per cent average monthly growth though reporting that the growth for June and July is below the average annual growth. It should be pointed out that an annual growth of 5 per cent is considered a significant one, while a growth of 10 per cent is unacceptably high. For comparison, the money mass in the Euro zone for the last 12 months is 7 per cent, which is considered a high growth, while in Bulgaria the respective growth is 28.3 per cent.

Table 10. Money supply (broad mon ey) in BGN billion, August 2004 г. – August 2005 г.

Month	08	09	10	11	12	01	02	03	04	05	06	07	08
Money	18.4	18.7	18.8	18.9	20.4	20.5	20.7	21.4	22.0	22.5	22.8	23.2	23.6
Growth		1.9 per cent	0.5 per cent	0.2 per cent	7.9 per cent	0.6 per cent	1.1 per cent	3.2 per cent	2.9 per cent	2.1 per cent	1.6 per cent	1.6 per cent	1.7 per cent

Source: BNB, Weekly monetary statistics

Therefore, a conclusion could be made with regard to the money supply, namely that the April regulation has not contributed considerably to the decrease of the rate of growth of the money supply. This should also be interpreted as a confirmation of the previous analysis for the inefficiency of the regulation.

The preceding analysis of the credit expansion in the banking system as well as the necessity for retention of the credit growth are supported by the recently published report of the International Monetary Fund (IMF) for the global financial stability. The statistics presented in the IMF report show that Bulgaria is second in terms of credit growth in newly emerging Europe. The average credit growth for the last three years in Bulgaria is 46.8 per cent. This growth is three times bigger than in Greece for example, which has the largest credit growth among the Western European countries. The average credit growth in the newly emerging Europe is 27.7 per cent. In contrast to the rest of the countries, where lending increases rapidly, the share of non-performing loans in Bulgaria is higher – 7.1 per cent. With regard to credit growth in the region, Bulgaria falls back only after Belarus (70.2 per cent).

Of course, these statistical data should not be interpreted as a strict evidence for the excessive growth of the credit expansion. Bulgaria has still to make up for the indicator credit volume against GDP. The point is, this expansion is necessary both for the business and the population to stay within reasonable limits, beyond which the stability of the banking and financial system would be exposed to risk.

GENERAL TENDENCIES

The traditional summer ease, typical for the capital market in the country, did not skip the trade on the stock exchange for another consecutive year. In contrast to previous years the first two weeks of July could be defined as a period of consolidation following the continuous fall in prices during the second quarter.

Immediately after clarification of the political situation around the formation of the government, the prices of most of the companies restored their upward trend but this time in a much more cautious way compared to their sharp growth in the beginning of the year. As a result the stock exchange indexes started lightly to recoup their former values and SOFIX increased from 727 to 898 points though two days before the end of the period it exceeded the limit of 900 points. At the same time the relatively new index BG-40 even exceeded its highest value of 133.36 points, registered in the middle of March and reached 140 points.

Figure 18. Movement of SOFIX for the period 01.07.2005 – 30.09.2005

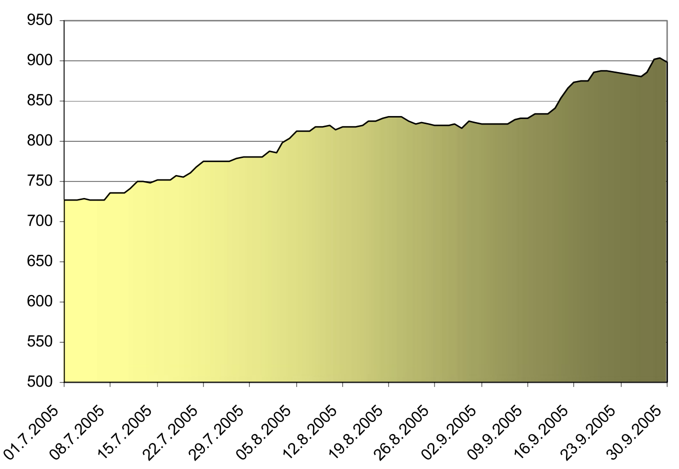
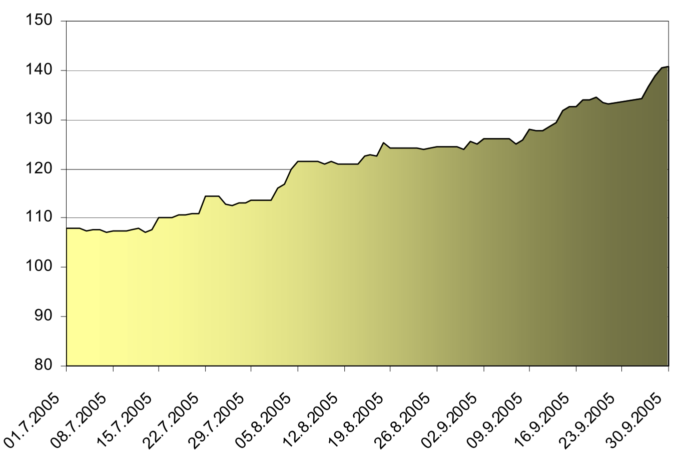


Figure 19. Movement of BG40 for the period 01.07.2005 – 30.09.2005



Notwithstanding the restored upward trend of almost the entire market or at least of the most actively traded companies, the registered movement of the indexes is still troubling as to the stability of the capital market. In the third quarter SOFIX increased by over 23 per cent and BG-40 by over 30 per cent following the fall registered in the second quarter by 13 per cent and 12 per cent respectively. Such sharp turns of the movements on the market are typical for the developing markets but has a negative influence on the investors` confidence as a whole and mainly internationally. Although the adjustment during the second quarter was expected to a great extent by the specialists, the increased volatility created uncertainty and endued the market with some chaotic characteristics.

The ease in trade was accompanied by ease in corporate events as well. On the one hand the annual general meetings of the shareholders were held and respectively, the companies preferred to wait for the major decisions after the summer holidays. Such a behavior is completely acceptable, especially if the company itself decides it needs more publicity with respect to the major events of its activity, which could not be achieved in summer due to low investors` attention. Supporting this statement is the fact that most of the companies that have decided to increase their capital, for example, took this decision in September. Two companies with special investment purposes were registered in the beginning of the summer i.e. "Park" SPV (special purpose vehicle) and "Advance Tarafund" that have received their licenses from FSC just before it.

In parallel with the above, the most actively developing market on the stock exchange that of the bonds continued its expansion. Five more bond issues were registered during the quarter including one issue of municipal bonds of Shoumen municipality and one mortgage bond issued by Economic and Investment Bank Ltd and a trend is observed the number of the bond issues to leave behind the number of publicly registered companies. Such an expansion of the bond segments is explicable since this market has been ignored for a long time as a source of funding and as a close alternative of the bank loans. On the other hand, notwithstanding the large number of registered companies, the image of the capital market is determined not by the bond issues but by the shares traded and the quality of the companies that have issued them.

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For the three months period, from July to September, three companies were deleted from the FSC register – "Bentonit"Ltd, "Komex" Ltd and "Neven" Ltd. The three companies were traded very sporadically before their exit and it could not be said that they were of decisive importance for the market but they supported the imposed opinion for the market weak efficiency and companies` lack of confidence that they could successfully fund themselves on it.

Two primary public share offerings were realized during the quarter, those of Web Media Group Ltd and of Stargen

Aquapharms Ltd. Although the funds raised by primary offerings are still small in size, similar companies are considered pioneers in primary capital raising and have a decisive importance in terms of the future development of the entire market.

This parallel process of registering new companies and deleting others leads to the more general conclusion that even slowly the corporate culture of the registered companies and the market itself changes towards larger publicity. The companies that exit the market either do not rely on the capital market or do not accept the obligations of the public entity. The newly registered companies with effected primary offerings have accepted their obligations and have become aware of the benefits of publicity and the advantages of parallel development with the entire market.

At the end of the quarter FSC licensed the first contractual funds in accordance with art. 164a of the Public Offering of Securities Act (POSA): TBI DYNAMIC, SENTINEL – PRINCIPAL and DSK STANDART. At 30th of September 2005 only the first one is registered on the stock exchange for trading but it is expected that their number will rapidly increase compared to the number of the investment companies due to the priorities offered by the funds mostly with regard to the decreased expenses under side activities towards their main investment activity. Similar funds in other countries accumulate considerable resources mainly from non-professional and individual investors and represent a major part of their savings. The expectations in Bulgaria are alike. Something more, due to its low liquidity, the market in Bulgaria reacts much more vigorously to the penetration of each new stronger institutional investor.

In the beginning of August the first adjustment of the BG-40 index base was done. BG40 is computed based on the issues of shares of the Top 40 companies graded by the number of transactions executed in the last six months. DZI Bank AD, Prouchvane i Dobiv na Neft i Gaz AD, Investor Bg AD, Advance Invest AD, Blagoevgrad BT AD, Bulgartabac Holding AD, Fazerles AD and Sofia BT AD dropped out from the index and the share issues of Bulgarian Telecommunication Company, KRZ, Odesos AD, Industrial Capital Holding AD, Holding Coop Yug AD, Polimeri AD, Razvitie Industria Holding AD, Mel Invest Holding AD and Hidravlichni Elementi i Sistemi AD were included. The envisaged frequent adjustments of the index give grounds for some criticism but on the other hand they help the proper reflection of the market movements. What is more, it is very optimistic to know that at the start of its calculation in the beginning of February, the index included share issues that concluded around 150 transactions for the six months period preceding February while during the adjustments in August the last company in the index set the limit to above 500 transactions.

Stock Exchange Trading

Market Capitalization

Capitalization on the stock exchange during the three months period marks a strong growth and exceeds BGN 9 billion at the end of September. The growth is by 7.3 per cent compared to the end of June but this to a great extent is due to the deletion of one of the largest companies under this parameter at the end of the second quarter, Lukoil Neftochim Bourgas AD. Still, growth is observed compared to the first quarter when market capitalization reached its highest values in the history of the stock exchange.

In this particular case a slight lack of balance is monitored between the growth of the capitalization on the stock exchange and the growth of the SOFIX index, which is also based on that parameter. The outstripping rate of growth of the index by 25 per cent against 7 per cent for the entire stock exchange is not typical for previous periods (if excluding the registration of the Bulgarian Telecommunication Company AD) and is surprising to some extent having in mind the increase of the prices of all the shares and not only those included in the index. On the one hand this gives grounds for criticism with regard to its representative character but on the other, shows a stronger interest in the items included in the index.

Irrespective of the above the actually traded capitalization is considerably lower due to the low free float of the companies registered on the stock exchange. The strong concentration of ownership is the main obstacle as to the market liquidity. The improvement of the market as a whole is one of the items in the strategy for the development of the capital market in the country.

Table 11. Market capitalization

Market capitalization	30.09.05	30.06.05	31.03.05
Official share market, segment “A”	123 770 590.75	113 699 897.35	48 124 419.20
Official market share, segment “B”	775 156 803.02	645 816 639.66	714 313 964.28
Official market share, segment “C”	1 440 137 155.72	1 178 390 108.27	1 317 507 266.34
Unofficial market share	6 751 007 881.87	6 535 227 706.27	6 659 298 901.85
TOTAL	**9 090 072 431.36**	**8 473 134 351.55**	**8 739 244 551.67**

Turnover, volume and liquidity

The turnover during the third quarter decreased by approximately BGN 72 million compared to the second quarter and reached BGN 278 million for all the markets representing a registered fall of near 25 per cent. Since the movement of the market for the period is ascending, this considerable fall could be interpreted only as a lower activity of the market players typical for the summer months.

Although the securities transferred during the period on the share market has almost doubled compared to the previous period, the turnover and the number of transactions has recorded a drop mainly due to the bigger number of package transfers of larger share volumes.

is additionally strengthened by the investors` disappointment after publication of the half-year bad financial results.

Table 12. Statistics of the market of BSE – Sofia for the second and third quarter of 2005

Market	01.07.2005-30.09.2005			01.04.2005-30.06.2005		
	Lots	Turnover (BGN)	Transactions	Lots	Turnover (BGN)	Transactions
Official share market, segment “A”	2 248 819	8 080 932,89	4 281	1 530 549	5 452 316,25	3 106
Official share market, segment “B”	968 700	6 772 472,20	1 598	764 245	4 793 789,19	1 247
Official share market, segment “C”	7 822 349	41 009 938,67	17 957	3 214 491	20 284 832,58	21 376
Unofficial share market	18 534 961	164 160 977,32	23 115	8 158 861	249 093 321,97	25 776
Unofficial bond market	28 905	48 851 301,51	124	20 984	34 224 757,66	146
Official market of corporate bonds	5 749	6 185 448,81	49	17 870	19 326 915,17	70
Unofficial market of other securities	781 898	185 446,60	149	1 842 229	429 087,88	223
Unofficial market of CI	28 093 115	19 569 054,97	4 221	53 519 597	36 210 716,29	16 057
Primary share market	645 731	2 782 070,46	72	135 902	154 822,96	37
Primary market of other securities	300 000	226 764,70	55	2 300 000	275 170,31	170
Total	**59 430 227**	**297 824 408,13**	**51 621**	**71 504 728**	**370 245 730,26**	**68 208**

Table 13. Average daily trading values on BSE-Sofia for the second and third quarters of 2005.

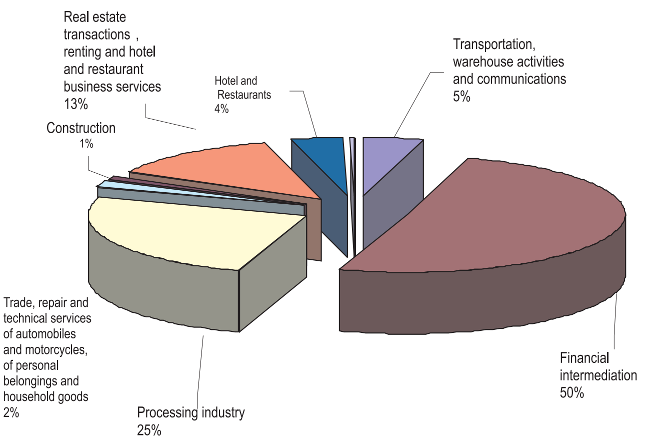
Market	01.07.2005-30.09.2005 г.		01.04.2005-30.06.2005 г.	
	Turnover	Transactions	Turnover	Transactions
Official share market, segment A	130 337,63	69,05	87 940,58	50,10
Official share market, segment B	109 233,42	25,77	77 319,18	20,11
Official share market, segment C	661 450,62	289,63	327 174,72	344,77
Unofficial share market	2 647 757,70	372,82	4 017 634,23	415,74
Unofficial bond market	787 924,22	2,00	552 012,22	2,35
Official market of corporate bonds	99 765,30	0,79	311 724,44	1,13
Unofficial market of other securities	2 991,07	2,40	6 920,77	3,60
Unofficial market of CI	315 629,92	68,08	584 043,81	258,98
Primary share market	44 872,10	1,16	2 497,14	0,60
Primary market of other shares	3 657,50	0,89	4 438,23	2,74
Total	**4 803 619,49**	**832,60**	**5 971 705,33**	**1 100,13**

The ascending movement of the share market during the quarter covered almost all actively traded issues. The main exception were the shares of the Bulgarian Telecommunication Company AD which following the share split of 1:35 in the middle of July recorded a slight fall. This movement is somewhat surprising as the Bulgarian market shows a tendency to be followed by all actively traded items, like BTC share, when it makes a turn in its movement. Obviously the telecommunication company moves in the opposite direction, as it has been the only not loosing investments during the continuous fall in the second quarter. The unconvincing performance of the shares of the company

During the third quarter more than 51 000 transactions were concluded representing a decrease by nearly 17 000 compared to the previous one. The number of the securities transferred recorded a drop as well though mainly due to the decreased liquidity of the compensatory instruments. The largest drop is in the turnover of the unofficial share market where most of the actively traded companies are registered, except for the holding structures. The fall on this market namely predetermines the overall decrease of the turnover of the entire stock exchange.

As a result of the drop of the general trade indexes the average daily values also decrease considerably. For the first time during the year the average number of transactions for a trading session is below 1000. Due to the decreased liquidity of the Bulgarian capital market and the strong influence on the turnover of the big block transactions it could be accepted that this parameter to a great extent is the most independent one and is the most representative for the stock exchange activity as it actually reflects the investors` aptitude for active trading.

Figure 20. Structure of trade per industries for the third quarter of 2005



The structure of the trade per industry is almost identical with the structure of the previous month. The slight increase in turnover is observed with companies dealing with financial intermediation (mostly holding structures) and those dealing with transportation and communication mainly at the expense of companies from the service sector. In the mid run it is not likely to observe a change in the current situation as there is no representation of all the industries in the country on the stock exchange or at least their correlation is not the same as it is in real economy. This is one of the main criticisms to the stock exchange and respectively one of the main steps in the strategy for its future development. As a result of the above if the capital market does not succeed to attract new structure determining companies from many and different industrial sectors for a longer period of time, the market will not be in a position to fulfill efficiently one of its main functions as a major indicator of the entire economic growth in the country.

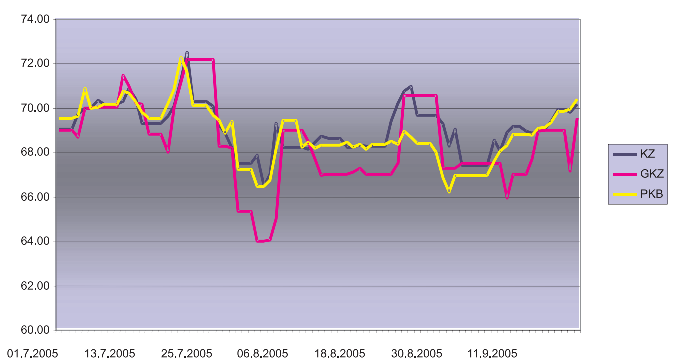
Unfortunately this is a very long process. The transformation of the stock exchange into a mirror of the economic activity is related to other factors as well mainly within the trading structure itself. For example, the privatization processes and the compensatory instruments have determined the market growth till now. In future, however, large privatization deals are not expected and the issue of compensatory instruments and their usage should be dealt with before the EU accession. With reference to the above the capital market should seek new supporting points for the future and if it does not succeed to find them it risks falling into a new lethargy which will drive back the new issuers due to the limited funding opportunities and risks to fail changing the sectoral structure of the registered companies.

Compensatory instruments

The compensatory instruments are one of the traditionally liquid items since their registration for trading in 2002 and one of the engines of the capital market. In the course of the quarter, the compensatory instruments trade registered its largest drop and the number of transactions fell nearly 5 times while the turnover twice. Such a decrease is not unexpected given the fact that the trade activity depends exclusively on the privatization process, which obviously dies away. Even the organized, centralized non-attendance public auctions could not influence considerably their prices or liquidity. This is partially due to the fact that the last several auctions lack attractive enterprises or that the Privatization Agency prefers to receive cash for those enterprises.

Despite the affected ease and the relative stability of the prices, as shown in the chart below, the problem still remains open and the government is mainly responsible for its solution. Till then, however, affected ease and further decreasing turnover are expected unless a privatization deal appears to restore active trading.

Figure 21. Movement of the prices of the compensatory instruments for the period 01.07.2005 – 30.09.2005



IT Development

Future development of the capital market in the country is unthinkable without lining it with up-to-date IT systems. Their implementation is an expensive process as far as software supply with respect to similar activities is done mainly to answer the needs of one organization not of the mass end users. Notwithstanding this, the future demand for IT products is very important for the market. The mass penetration in the capital market of the rapid links of communication leads to increased necessity of more quick and more effective disclosure of information by the public companies and the other issuers of securities. The increased market liquidity places further requirements on the trading systems and the possibilities for easy access on the part of the investors. The COBOS system for orders and agreements, filling the market niche two and a half years ago, quickly gained popularity but some shortcomings occurred. Because of that, in September the stock exchange finalized its initiative to offer an alternative access to the trading system through Internet that opens it to systems for communication designed by the stock exchange members to be used by their customers. Similar systems are maintained by many foreign intermediaries and play an important role in the efficiency improvement of the capital market and for its access but till now in Bulgaria they did not have the necessary resources for such development and the trading system itself did not allow it.

Apart from its main role as an alternative access to the market and information distribution in real time, this additional module has another advantage. The increased process of globalization in the last few years inevitably will influence Bulgaria as well and the capital market in particular. In that respect it may well be that foreign intermediaries enter the local capital market especially after the last amendments to POSA regulating the mutual recognition of the licenses for investment intermediation.
It is very probable, however, that they will prefer to use their own solutions as to the e-trading and servicing of customers. Namely, the putting into operation of such a module could guarantee the safe and rapid access to the market and the information generated on it and respectively to improve the quality of the investment services offered.

Legal framework

In the beginning of 2004, the Parliament approved at first reading the Law on Promoting Investments in SMEs but it never reached second reading and adoption. A lot of criticism was expressed during the debates around some controversial items in the law mainly on the part of the current ruling majority. They were mainly with regard to the necessity of interference of state in the activities of the companies for risk financing as the law envisaged allocation of funds from the budget and guarantee the payments under the bond issues of those companies. A year and a half later there is still no clarity as to whether the law will be approved or not.

Part of the small and medium size enterprises have received the needed financing as bank loans. The restrictions on the credit expansion will influence their ability to receive such financing in the future. From this point of view it is reasonable to consider the possibility for adopting the law after calculating the expected benefits from the existence of companies for risk investments.
In parallel their licensing with FSC and the trade with shares issued by them on the stock exchange could attract the interests of longer-term investors.

The oil "tsunami" raging at international markets swept over Bulgaria as well.
The prices of all oil-bound energy resources went up. Expected increase effects include higher inflation and delayed economic growth.

Government policy priorities were declared against the background of discussions on new energy prices. We can synthesize these in three basic categories: restructuring, privatization and Belene NPP.

The construction of a new nuclear power plant will continue according to the schedule approved by the ex-Government. The role of the State in the project is not yet elaborated. Privatization of big energy sector companies will continue, but first a new restructuring model has to be found. It should guarantee a competitive Bulgarian energy sector within the Single Market.

Government Policy

The new Government started with changing the structure of the Council of Ministers. The Ministry of Energy and Energy Resources and the Ministry of Economy were merged into the mega-structure of a Ministry of Economy and Energy. Responsibility for the ministry was delegated to Minister Rumen Ovcharov. Such a structure would make sense if it leads to improved efficiency of government administration and to lower administration costs. The latter will become clear when next year government budget parameters become known, while efficiency can be assessed only in a mid-term perspective.

Government's intentions to reckon with undertaken commitments to the EU regarding the small units of Kozloduy NPP became apparent upon the presentation of the new Cabinet. However, Government's intentions with respect to the big companies in the sector were not made clear. According to the minister, NEK and Bulgargas will be sold upon restructuring. Yet no one knows what the restructuring model will be and whether previously agreed time limits will be observed.

As CED projected in its previous report, the construction of Belene NPP remains a priority for the new Cabinet. The minister pointed out that project work will progress according to the schedule approved by the ex-Government.

Electricity Market

The free market segment in which sellers and buyers close deals for the sale of electricity at negotiated prices continues its development at a slow pace. In early July, companies with annual consumption of not less than 20 Gw-hr were admitted to the free market. Since 1 July 2006, the threshold will be lowered to 9 Gw-hr. However, this is only administrative opening. In July and August, total companies exercising their right to directly negotiate electricity prices increased by two only, despite the serious increase of the number of privileged companies from 1 July 2005.

Total traded electricity quantities remain at previous levels, at about 50 Gw-hr per month. An upward trend is observed in the deficit price dynamics on the balancing market for electricity. In July, prices varied between BGN 70.86/Mw-hr and BGN 91.80/Mw-hr. Despite that, it is still more profitable for producers to sell electricity on the regulated market. On the other hand, privileged buyers' unwillingness to buy at negotiated prices can mean two things: (1) companies, qualified as privileged consumers, are not aware of the springing opportunity, or (2) they do not have human resource capacity to benefit from the opportunity.

Natural Gas Market

According to the new leadership of the energy sector, natural gas supply and transit prices may be renegotiated with Gasprom. Very important for the State and the economic agents will be the level at which new prices will be fixed. This concerns mostly enterprises with high share of gas consumption costs in total costs. The importance of such renegotiation results from the fact that Bulgargas is the only possible natural gas supplier in Bulgaria, in other words, the price increase will affect 100 per cent of consumers.

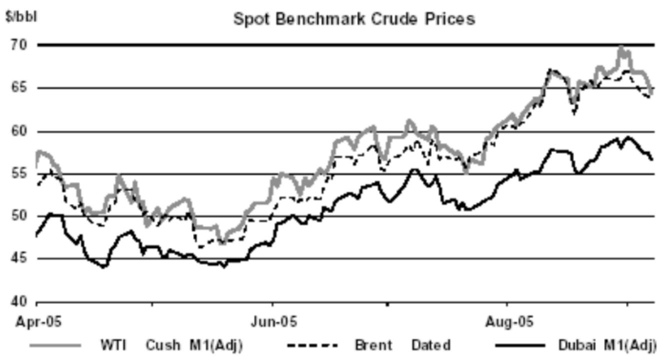
Important for the future development of the natural gas market was the appointment of a concessionary for the Danube Gas Distribution Region. Thus, regions with appointed investors are now four, as many as the regions for which notices for tender are expected. The other regions are attractive for concessionaries in terms of the large number of potential consumers. Despite the general rise of energy prices, one can project that natural gas will remain a competitive future alternative.

Energy Prices

Oil. Oil prices are still going up. At the end of August, Brent oil prices reached US$ 70 as a result of increasing demand and the difficulties exporting countries experience in increasing the production capacity. Furthermore, the bad weather in the Gulf of Mexico was a factor with very strong effect on the oil market in the past few months. Devastating hurricanes disturbed the supply, forcing the oil refineries in the Gulf to stop work.

This trend had effect on domestic market fuel prices. Besides the increase of international oil prices, domestic fuel prices were influenced also by the dollar exchange rate. Since the beginning of 2005 the dollar has restored, in a manner, its positions and in early September it was traded at levels of BGN 1.60 for 1 US$. In the event of a future appreciation of the US currency, the negative effect of expensive oil prices on the development of the Bulgarian economy will increase.

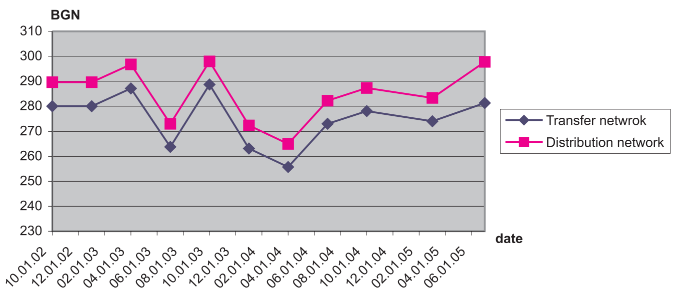
Figure 22. Spot Crude Oil Price Dynamics for WTI, Brent and Dubai Grades



Source: Monthly Crude Oil Price Report, International Energy Agency, September 2005.

Natural Gas

Figure 23. SERC-fixed natural gas prices in BGN/1000 m3 for consumers connected to transfer and distribution network



The obvious correlation of oil and natural gas prices will call for higher prices since 1 October. This, in turn, will have effect on the costs of the most gas-intensive industries. In Bulgaria, these are the chemical industry with a share of 37.28 per cent in total consumption, the energy sector with 33.5 per cent and metallurgy with a share of about 11 per cent in total natural gas consumption. The effect of higher gas prices on finished product prices depends on the share of gas in production costs and on the price elasticity of the goods produced by such enterprises. The higher the price elasticity of a product, the higher share of the cost increase will have to be born by the producer at the expense of his profit.

Electricity. Recent discussions on electricity prices have been particularized. SERC declared its intentions to increase since 1 October electricity prices for industrial medium voltage consumers by 5 per cent and for industrial high voltage consumers – by 16 per cent. This increase results mainly from Government's commitments undertook upon the sale of EDCs. It is certain that upon increase of electricity prices, the enterprises in the above two categories will increase their electricity costs. Enterprises with high share of electricity costs in total costs would have reasons to increase the prices of their products. However, thinking that all enterprises have reasons to increase their prices is wrong. The majority of companies in this category most likely incur electricity expenses for office purposes only. Interestingly, a large portion of the companies eligible to directly negotiate electricity prices with the sellers do not do that, but when prices on the regulated market go up, everybody is ready to protest.

Sector Priorities

There will be electricity producers trying to justify their costs before SERC and consumers who, on the contrary, claim that prices are high, until sufficient liberalization of the electricity market is achieved.

With that end in view, the State should minimize the free trade barriers in the sector. Besides accelerated removal of free trade thresholds, there is also a need to eliminate the requirement for payment of all obligations towards NEK. To become a privileged consumer, a company must have paid all its obligations to the state electricity transfer company. While there are enough mechanisms in place to settle intercompany obligations, such kind of government intervention is not reasonable. Besides, the opportunity to reduce electricity costs by direct negotiation would make companies more efficient in paying their obligations towards NEK

In the gas distribution sector, there is a need to speed up the tenders for concession of the other gas distribution regions. Before tenders are organized, it will be good to investigate the conditions at which they could be attractive for investors. We have seen tenders fail because of lack of interest, which ultimately delays the whole process of Bulgaria's gasification. The initiative to work out a development strategy for the sub-sector is not without reason. It will accelerate the process of Bulgaria's gasification and will confirm country's positions in the implementation of international projects like those for the construction of gas pipelines passing through Bulgarian territory.

Regarding nuclear energy, it has become clear that renegotiation of undertaken commitments to the EU will not yield positive results. Efforts in this field should be focused on the construction of Belene NPP, while finding the optimum combination of responsibility, risk and yield for the State and for the possible private project partners.

Regarding electricity production, the Government should focus on well-timed implementation of the rehabilitation and privatization projects for the big thermal power plants (TPPs).

Floods incurred enormous damages to transport infrastructure. The new Government declared its transport priorities: safety and security, modernization and higher quality of provided services. The Ministry of Transport plans to set up a national transport system and to intensify the dialogue with the business.

Flood losses. Heavy summer rains caused serious damages to the road infrastructure. According to a Ministry of Transport report, road structure rehabilitation will cost BGN 106 m. BDZ (Bulgarian State Railways) also incur heavy losses from unrealized haulage. CoM extended a grant aid of BGN 30 m for emergency rehabilitation of some railway infrastructure projects from the Public Investment Projects Company set up during the term of office of the previous Government. The new minister said in an interview that railway transport tariffs will not be increased. This means that the two state companies will have to finance their losses either from higher subsidies from the state budget, or by reallocating own funds budgeted for other activities.

Government policy. The Ministry of Transport declared the priorities of future management:

- Transport system safety and security;
- Transport system modernization;
- Accelerating projects financed from the pre-accession funds;
- Improving the quality of transport services – developing a national transport scheme integrating the different transport sectors;
- Enhancing the dialogue with the business.

Declared priorities are well formulated, but need particularization with a view to become meaningful and implementable.

Railway transport. The new Cabinet announced some more specific intentions for this sub-sector. The set up of a railway holding and BDZ's penetration in the road transport are the events, which will have the most pronounced effect on sector development. The new government plans to amalgamate in the holding the infrastructure company and BDZ, possibly including also the locomotive maintenance company.

The basic arguments for the ministry to amalgamate the infrastructure and the carrier include: (1) the high losses which BDZ incurs from paying infrastructure charges and (2) the negligible number of private railway carriers. The latter, however, results from the needlessly high infrastructure access charges, which block the entry of competitors, and not, as claimed, from the fact that the companies exist separately. It would be interesting to see the financial results of the infrastructure company with a view to establish the rate of return at which it operates and whether collected charges could be decreased.

The set up of a holding structure could improve the operational efficiency of the private sector. Such structures are characterized by management concentration, which should improve decision making efficiency and allow for economies of scale to be achieved. The cost of capital attracted for the holding would be lower, because the holding will have higher financial stability compared to the companies taken apart, which will lower the risk and, hence, creditors will demand lower interest on loans. Optimization of tax liabilities is possible within a holding structure.

However, viewed in a governmental perspective, the holding may have negative aspects, for example, possible cross-subsidization. In such a situation, loss generating activities will be financed again from profit-generating ones, instead of improving their efficiency or liquidating them.

Road transport instead of loss-generating lines is a good idea launched by the new ministry. Using microbuses for lower-traffic or loss-generating lines will generate sizable economies. Thus the State will still perform its social functions, while limiting losses without increasing the price of the service.

Praiseworthy is also Government's intention to work out a sector development strategy and to define clearly the role of the State in the sector.

Air Transport. The two opposite trends in this sector remain clearly outlined. While air traffic flow increases, development of airport capacity registers delay.

In the first six months of 2005, growth in the passenger flow at the airports of Varna, Sofia and Burgas stands at 20, 19 and 15 per cent respectively, remaining at high levels for a couple of years now. Indicative of the growth in travelers "to" and "from" Bulgaria is the emerging new low-price carrier – "Wizz Air".

At the same time, the concession for the two Black Sea coast airports is still under litigation. The main contractor under the project for Reconstruction, Development and Expansion of Sofia Airport – Strabag announced that project completion will be delayed. A realistic deadline for putting into operation of the new terminal and the related service facilities is early to mid 2006.

Priorities

To accelerate transport sector processes, the new Government should make the sector complete. This will be achieved when the Road Executive Agency is transferred from the Ministry of Regional Development and Public Works to the Ministry of Transport. That will make possible an integrated sector development policy which requires better coordination and efficiency.

Privatization of big state companies like NMB (Navigation Maritime Bulgare) and Bulgaria Air should be accelerated, while employing competition-generating market methods.

Launched sector projects should be completed within initially negotiated time limits, while holding partners responsible for possible delays or deviation from undertaken commitments. With that end in view, all future projects should be awarded at full transparency of the procedure and with clearly defined responsibilities and obligations of all partners.

Transparency and publicity of operation should be achieved for the other state companies in the sector, like BDZ and NC Railroad Infrastructure. The amalgamation of these two companies into a holding structure will produce opposite effects.

The third quarter of 2005 did not bring any significant developments in the Bulgarian high technology and communications sector. The new Government has declared priorities which largely continue in the path of ex-Government initiatives. Perhaps the most important fact with serious effect on future ICT sector development will be the tenders for individual license for point-to-multipoint type networks.

Individual licenses for point-to-multipoint type telecommunication network. At the end of July, the Communications Regulation Commission (CRC) took decision to announce two tenders with secret bidding for issuing five individual licenses for carrying out telecommunications through networks of “point-to-multipoint” type with frequency resource in the range 3.4 – 3.6 GHz.The licenses are with national coverage and will be issued for a term of 10 years. Two of the licenses will be of class A and will provide a limited frequency resource of 2 x 21 MHz, and the other three will be of class B and will provide frequency resource of 2 x 10.5 MHz each.

The tender for issuing of the two class A licenses took place on 11 October 2005 at initial tender price of BGN 1 344 000 per license and bidding step of BGN 100 000. Six companies submitted tender documents – Mobiltel AD, BTC AD, Nexcom – Bulgaria EAD, Trans Telecom OOD, Cablenet EOOD and Carrier BG OOD. Following a two-day bidding, Trans Telecom OOD and Cablenet EOOD were appointed successful bidders with a proposal of BGN 5 044 000 – a remarkably high price, given the volume of the Bulgarian communications market. According to experts in the field, achieved prices are high even for the developed European markets (for example, prices of similar tenders in Norway /November 2004/ and Slovakia /May 2005/ were lower, given the provided frequency resources and the population of the respective country).

The tender for issuing three class B licenses will take place on 25 October 2005 at initial tender price of BGN 672 000 and bidding step of BGN.

The “point-to-multipoint” type telecommunication networks are used for provision of different telecommunications services such as transfer of voice and data, Internet access, fax, telex, video information and multimedia applications. The technology allows the support of broadband data transfer with rates between 128 Kbps and 34 Mbps.

The main advantage of the “point-to-multipoint” type wireless networks is the possibility to provide fibre optics quality services to locations, where the installation of fibre optics is practically impossible or economically ineffective. This gives the possibility to construct networks in sparsely populated as well as in strongly urbanized areas and makes the band extremely appropriate for public data transfer networks with national coverage.

Bulgarian projects for World Summit Awards. The Bulgarian projects which will represent the country at the annual competition for the most prestigious world electronic content award - World Summit Award, were selected at the end of July. The 2005 competition is organized in eight categories: e-learning, e-culture, e-science, e-management, e-health, e-business, e-entertainment, and e-integration. Twenty one projects in seven categories were submitted (there was no project in the e-health category). Approved projects include:

- e-integration: the project iCenters - www.icentres.net
- e-entertainment: the game Chi:Kho – www.chikho.com/game
- e-learning: electronic learning platform of the Medical University, Sofia – http://mu-sofia.bg/
- e-culture: the portal Discover Bulgaria - http://www.discover-bulgaria.com/
- e-management: Management Information System in MoF for ISPA projects - https://ispa.minfin.bg/
- e-business: software product for cell phones Advanced Call Manager – http://www.webgate.bg/products&rmenu=1&rsmenu=1

The following criteria were applied in project selection: value added for consumers and project’s relevance to a problem; quality and richness of content; user-friendliness; attractive design and level of technical implementation.

Priorities of the new Government. The new Government officially declared its political priorities in September. Within the measures for improving the productivity and competitiveness of the Bulgarian economy, the Cabinet will make efforts along several lines: creating an efficient mechanism for encouraging innovations and the use of information technologies; modernizing science in line with Lisbon goals; increasing government expenditure for science; encouraging corporate investments in research and development, while changing science financing principles.

Overall, above priorities follow the logic of ex-Government’s ideas. Since a couple of large-scale projects for modernization of IT in education and encouraging the IT acceptance by companies and the people were started in the past one and a half year, the new Government only has to continue in the trend and successfully fulfill the goals set.

One of the first steps of the new Government was to set up a **State Agency for Information Technology and Communications (SAITC) –** a second-level spending unit at the Council of Ministers.

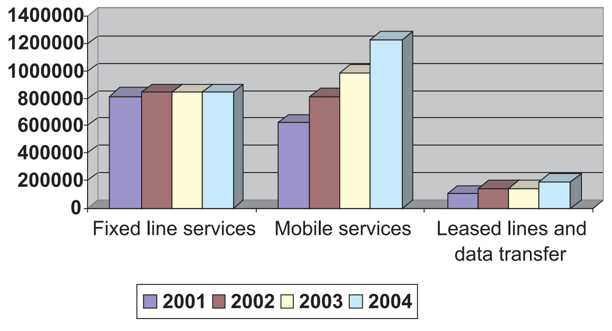
The Agency should guarantee a free and independent communications and information technology policy. It will be staffed with officers from the Communications Policy and Information Society and Information Technology divisions within the Ministry of Transport and Communications.

The activity and organization of SAITC will be regulated in rules on its structure to be approved by the Government along with the other secondary legislation pertaining to the change within one month after the decree takes effect.

According to the appointed director of the Agency, a priority of SAITC will be to create a favorable environment for encouraging companies from the legal business. The Agency envisages appointing of "electronic" ambassadors of Bulgaria worldwide and has already designated the one for the USA - the President of Internet Society – Bulgaria, Veni Markovski. Ambassadors will have the task to attract to Bulgaria big foreign companies for implementation of joint projects with Bulgarian companies. The Agency will consist of a couple of divisions responsible for ICT development in different sectors like healthcare, education and other.

Bulgarian telecommunications market. CRC's 2004 report was officially presented in July. According to the report, 2004 Bulgarian telecommunications market volume stands at BGN 2.503 b, registering a growth of 13 per cent against 2003. In 2004, the share of the Bulgarian telecommunications market in total GDP is about 7 per cent, outpacing again GDP growth.

Figure 24. Structure of the Bulgarian telecommunications market (thousand BGN)



Source: CRC, 2005

Expectedly, in the last four years mobile services register sustainable growth, whereas in 2004 fixed line services register slight decrease compared to 2003. While in the past year penetration of mobile services in Bulgaria registers notable growth and stands at 65 per cent, it still remains low compared to Community levels. The large number of subscribers of pre-paid mobile services – 2/3 of total subscribers – should be noted.

ERP systems on the Bulgarian market. According to data by CBN Pannoff & Stoytcheff, as of mid-2004, ERP (Enterprise Resource Planning) system installations in Bulgaria stand at 300, including 2/3 in the small and medium-sized enterprises sector. Expectedly, companies owned by foreign investors register the highest number of implemented business management systems. Industry takes the lead by number of information system installations, followed by trade and services. The Industrial sector is the leading one in number of installations of information systems, followed by commerce and services!!!

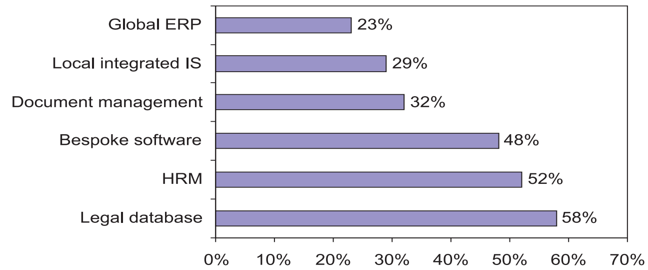
According to CBN data, in the period 1996-2005, active market actors include 22 ERP system developers represented by 33 system integrator companies.

To date, the Bulgarian ERP market can be divided into three segments – top products, medium market products and products for small companies. Third segment products are developed mainly by Bulgarian companies and provide limited functionality for small offices. Solutions for the medium market provide integrated finance, distribution, services and production management functionality for companies with more than one office. Leaders in this segment are the products of Maconomy, Microsoft Navision and Scala. Top products provide companies with full functionality and integration of all business processes. Leaders in this segment are Microsoft Axapta, Oracle and SAP.

Along with ERP solutions, CRM (Customer Relationship Management) products are enjoying recently increasing demand in Bulgaria. Since Bulgarian companies are improving their vision of the important role of the customer in the business relationship, one can expect notable growth in the market of such software solutions in the next couple of years.

A CIO Magazine survey of the spread of information solutions in companies reveals that the Bulgarian ERP and CRM market is yet to develop in a close perspective.

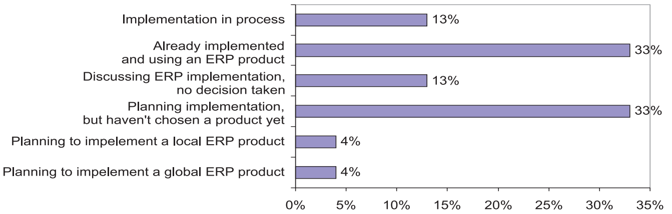
Figure 25. Information systems in Bulgarian companies



Source: CIO Magazine, March 2005.

Figure 25 shows that legal information systems are still the most widely used, and according to Figure 26, more than 1/3 of interviewed companies plan to implement ERP in the near future.

Figure 26. Implementation of ERP systems



Source: CIO Magazine, March 2005.

In the third quarter of 2005, tourism development continued at a high pace. It is the high season of biggest profits for this sector of the Bulgarian economy.

Number of Tourists and Revenues from Tourism

In the period January – end of August 2005 ***the number of foreigners*** who visited Bulgaria for holiday and rest is above 3 m, up 4.03 per cent against the same period of last year. In August 2005 alone, the number of tourists stands at 798 thousand people or up 7.4 per cent on August 2004.
The European countries, particularly EU members, remain a major market of Bulgarian tourist services. The share of tourists from these countries in total foreign tourists is above 50 per cent. Tourists from Ireland (121 per cent) and the Netherlands (51.48 per cent) register the highest growth. The number of tourists from Great Britain, Spain, etc., increases at a high pace.

Bulgaria restores its positions in the countries of Central Europe – Poland (total tourists above 95 thousand), Czech Republic (110 thousand), Slovakia (80 thousand), establishing an upward tend. The number of tourists from Russia registers increase after some delay in recent years and stands at 149 thousand people, or up above 10 per cent.

At the same time, in July alone, the number of German tourists, who are traditionally the largest group in the Bulgarian Black Sea resorts, is down 3.4 per cent. Construction works in the big resorts, which continued after the start of the high season, are stated as a major reason. Some growth in the number of Germans is registered in August when Germany took the lead by number of tourists with 428 thousand, followed by Greece with 426 thousand, Macedonia, Serbia and Montenegro, Great Britain, and other.

According to BNB's data, as of end of July, ***revenues from international tourism*** amount to more than EUR 1 b, or up 10.2 per cent on the same period of last year.
In the first seven months of 2005, Bulgarians' ***spending*** on travels abroad stands at EUR 438 m, or up 4.7 per cent against the same period of 2004.

The number of foreign tour operators, who offer Bulgaria as a tourist destination to their clients, increases. However, expectations about ***permanent boom*** in tourism were not fully justified – early summer season data do not confirm the optimistic projections of two-digit growth, which were based on ***the huge investments*** in special infrastructure and the doubled number of beds in some resorts.

The number of ***Bulgarians*** who prefer national Black Sea resorts increases as well, owing to a noticeably ***more flexible policy*** towards Bulgarian tourists in recent years, which gradually closes a serious gap. Although insufficient, efforts along these lines are a good start for attracting more Bulgarian tourists. They are generally better consumers of tourist services compared to foreigners where lower-bracket categories prevail. There is increasing supply of all-inclusive and at-last-minute offers at favorable conditions, which attract more Bulgarian tourists.

Investments in Tourism

Southern Black Sea Coast

Recent years have brought huge inflow of investments in tourism, which, by expert evaluation, go beyond reasonable limits. Construction and oversupply of estates along the Southern Black Sea Coast continues. Sunny Beach, holiday village St. Vlas and Ravda are now interconnected and the region is densely built up. Unfortunately, despite existing infrastructure problems, the building of new holiday villages continues – a large tourist complex is under construction in Ravda.
The area around the village of Chernomorets and Vesselie Campsite is going to be built up.
A new village Santa Marina is going to be built near Sozopol.

The above events have a couple of negative effects – enormous oversupply, which the market cannot absorb; lower real estate prices; disturbed ecological balance; the existing infrastructure cannot cope with the enormous bed capacity; which, ultimately, puts off tourists who cancel bookings.

In a mid-term perspective, the resorts south of Burgas may well become more attractive, provided, however, that future construction be done in a reasonable way. Low construction is currently prevailing south of Burgas, higher green area standards are applied – a component, which is indispensable for such resort complexes intended for holiday and rest. That is why investors focus their attention on this part of the Black Sea Coast.

North Black Sea Coast

Kranevo

The village provides good opportunities for special infrastructure development. Construction of new hotels with total 15 thousand beds is anticipated in the resort village of Kranevo in the next two years. Currently the village has about 17 thousand beds including only 7 thousand categorized ones. Before the anticipated expansion of beds, however, there is a need to reconstruct and expand the existing infrastructure. Otherwise, the problems of villages like Ravda, Sinemorets, Golden Sands and others, where the available water-supply and sewerage infrastructure does not have capacity to cope with the huge inflow of tourists, will be reproduced. Opportunities to finance the road infrastructure from European funds, particularly from SAPARD, are investigated.

Along the North Black Sea Coast, *Kavarna* also emerges as a village with good investment opportunities and development perspectives, provided, however, that construction is kept at moderate levels. Some people fear that the small town, which is one of the most attractive cultural centers along the Black Sea Coast, may turn into a residential complex like Mladost and Ljulin.

Shkorpilovtsi

In August, the Mayor of Shkorpilovtsi announced a very ambitious project for making the municipality the biggest resort along the North Black Sea Coast. The plan is to build a resort zone in the region with 25-30 thousand beds and to excel Golden Sands. Investors from Italy, Belgium and Switzerland show interest in the project. The zone will spread over 2.5 thousand decares. The region boasts with mineral waters, which will allow using the base all year round and developing spa tourism. Construction of a yacht port and a golf terrain is envisaged, as well as of an “inner sea” – a huge water pond, which will take water from the sea.

However, the implementation of this project still sounds like a dream, because it is largely dependable on the future construction of Kamchijski Pjassatsi water main the timing of which no one knows.
The project seems very attractive, but many tranquility and clean nature lovers may be disappointed, since tranquility and clean nature are the region’s beauty and attraction. Building a big resort complex may well ruin the spell of this untouched yet Black Sea Coast region.

Russian investors show permanent interest in Bulgarian tourist sites. A project for a international children’s recreation center in the *Kamchia* region is well under way – a large investment program of EUR 13 m will be started towards building a new hotel, open-air pool and a holiday village of single-family houses.

Investments in Winter Resorts

Bulgaria confirms its positions as a ski tourism destination of the day for the European countries, particularly for Great Britain. In the past season, the Bulgarian ski resorts registered the highest growth in this country compared to the other foreign resorts. Overall, registrations for Bulgaria are still low, but their growth is one of the highest. In the past winter season, 2.8 per cent of 1.1 m British tourists came to Bulgaria against 2.1 per cent for the winter season 2003-2004, registering an increase of about 10 thousand people. Comparatively low prices remain a major advantage of the Bulgarian winter resorts. The British tourist profile shows that skiers coming to Bulgaria are mainly beginners and the ski tracks in the Bulgarian resorts are comparatively short and easy. Guests from Great Britain are the biggest group in Bulgaria’s winter resorts. Balkan Holidays is the tour operator bringing the highest number of British tourists to Bulgaria (16 thousand in the past winter seasons); other tourist agencies in the sector include Crystal Holidays, Thomson, Thomas Cook, Ingams, Nielson and other. French resorts dominate the market of ski-tourist services in Great Britain, followed by Austria and Italy.

Active preparation of winter resorts for the new season is going on.

Bansko

Intensive construction and preparations for the new season is going on in Bankso, and the town will open the season with a total of 100 hotels. Some 50 new projects are under construction, including 11 hotels. Many new residential buildings, holiday villages and other are being built. Three-star hotels prevail. Like in the big resorts, problems include again lack of sufficient general infrastructure to absorb the construction boom.
Growth of tourist visits to Bansko in the winter season is projected at about 5 per cent. However, one notices again the paradox typical for summer tourism – doubled number of beds but rather small increase in the tourist flow. Given the huge investments, growth in the number of tourists should have been much higher, which indicates lack of good marketing strategies to attract tourists.

Borovez

Construction in Borovez intensified in the past year. In fact, the ambitious Super Borovez project has started. Six new hotels with total 800 beds are under construction. At present, new hotels are built in the central part of the complex near Rila and Samokov hotels and the first station of the gondola lift. Construction is expected to expand towards Beli Iskar and Govedartsi. Yet ecologists from Samokov and the region warn that the provisions of the project approved in the past year are not observed – in their opinion there are many changes and violations, which will do harm to the environment and disturb the ecological balance.

Pamporovo

Pamporovo also enjoys sizable investments. Russian companies are about to buy and modernize Persenk Hotel. Bulgarian companies from the region strive to attract investments from Western Europe and, lately, from Russia. The focal point is the region of Smolian where investments will considerably improve the tourist infrastructure – building new lifts, children’s camp, etc. Smoljan will come out with its own exhibition stand at one of world’s biggest tourist exhibitions to be held in Moscow in December, which will enhance the interest in the region.

Cultural Tourism Development

Cultural tourism, which is a key development opportunity for many Bulgarian municipalities, is increasingly in the focus of attention. Some municipalities have developed strategies and projects for the promotion of cultural tourism. Unfortunately, this form of tourism suffers very much from the lack of adequate road infrastructure and tourist centers in these Bulgarian regions. In 2004, investments in cultural-and-tourist centers amounted to only EUR 0.5 m. In the past year revenues from cultural tourism amounted to only EUR 170 m, or a negligible portion of total revenues from tourism. Encouraging signals come from some Bulgarian municipalities, which have made it their object to develop alternative forms of tourism. Foreign investors show great interest in the construction of four- and five-star hotels near unique cultural sights.

Government Policy in Tourism

Government policy outlines a couple of ***key priorities*** – encouraging local and regional initiative and promoting public-private partnerships. These are expected to contribute towards decentralization by horizontal cooperation of the State, local governments, branch organizations and the private sector. That will improve the dynamics of regional development and will create new jobs at municipal level.
The cultural-and-tourist information centers in Varna, Vidin, Polviv, Veliko Turnovo, and Russe were set up with that end in view.

The new government will take tourism out of the structure of the Ministry of Culture where it "stayed" for a while with the idea to achieve a symbiosis of tourism and the presentation of Bulgaria's cultural and historical heritage. The idea, including the opportunity to transfer funds from tourism to cultural initiatives and events, which, in turn, could attract tourists and boost the development of special forms of tourism parallel to sea and winter tourism, is not totally senseless. It seems, yet, that it would not be realized this way. However, there is still a need to combine different forms of tourism for the purposes of diversification and with a view to make Bulgaria an all-year tourist destination, which is vital for the country as well as for the different municipalities.

A State Tourism Agency will manage tourism and Ministry of Economy and Energy will be the spending unit of budgetary funds.

Amendments to the Tourism Act were passed in September. They envisage equal price levels for Bulgarian and foreign tourists.

Over and Over Again on Problems of Tourism

We have commented many times the problems of tourism, yet, unfortunately, some of them aggravate. As we have noted, the key problem is ***the poor quality of infrastructure*** – road, water supply, sewerage, water treatment and other.

Another major problem is ***the shortage of labor*** and unqualified labor. It will create serious future problems for Bulgarian tourism and will deteriorate its competitiveness.

Until recently, cheap labor preconditioned sector development, but shortage of qualified labor is becoming a serious problem. Young people with specialize tourism education leave the country to seek better opportunities and higher pay abroad. The "explosive" development of hotel resources was not accompanied by adequate human resource development in the sector. In fact, the expansion of hotel resources is divorced from labor market dynamics, location and structure. At present, Bulgaria is trying to develop modern tourism in the absence of one of its key components – qualified labor.

To solve the problem, one needs to have in place "healthy" working environment – providing opportunities for professional and career development and for assuming more responsibilities, promoting initiative, etc.

We have discussed many times unregulated ***construction*** and the overabundance of special infrastructure in big resorts. Clearly, it is impossible to use the full potential of this infrastructure; there is huge supply and lack of adequate demand; the environment is destroyed and the ecological balance is disturbed; there is shortage of general infrastructure, etc. Unique natural resources have been destroyed. In fact, the tourist complexes are highly urbanized, overpopulated, polluted, and noisy.

One should add to the above Bulgaria's ***insufficient popularity*** as a tourist destination, particularly with respect to the opportunities the country provides for cultural, spa, rural tourism. On other words, there is lack of adequate advertising and marketing practice. Most entrepreneurs in the sector still rely on intuition, will and enthusiasm; they do not operate with the necessary professionalism and with the appropriate tools.

Excessive construction in the Black Sea resorts leads to ***lower prices*** of holiday packages. To be booked up, tour operators and hoteliers are forced to sign next year contracts at lower prices compared to the current year. Rates will be probably cut by 3-4 per cent. Tour operators and Bulgarian hoteliers make efforts to attract tourists since late spring – April and May, which will lead to still lower prices in that period compared to the high season.

Lower prices, which attract, respectively, ***foreign guests with lower purchasing power,*** are the one alternative for Bulgarian tourism development. The other is to look for ways to develop forms of tourism other than mass tourism – more individual tourists, offering them specific forms of tourism like hunting, yachting, adventure, cultural, and other. This is the way to attract wealthier tourists to Bulgaria.

The above issues have reference to the strategic visions about Bulgarian tourism development. A good variant may be ***to combine the different tourist product forms,*** which will lead to all-year use of Bulgaria's natural resources.

Good Practices and Partnerships in Tourism

Competition in tourism has enhanced in recent years. Hence, countries have to join their efforts with a view to preserve and expand their positions on tourist markets. For example, in the past month ***the tourism ministers of Turkey, Syria and Egypt*** signed a common tourist zone agreement. The three countries will be presented as a single tourist destination on distant markets. Of course, that will give them an advantage and will improve their competitiveness. It is also a challenge to the other countries, including the Balkan states, and an example of good practice. The latter implies cooperation and finding common solutions and joint action forms to present the Balkan region.

An endeavor to join efforts was made in September with a meeting of tourism companies from the Balkan countries organized in Ohrid, which ended with the set up of ***Balkan Federation of Hoteliers Associations***. The meeting provided a forum for discussion of problems concerning prices, the visa regime, categorization in tourism, etc.

The border regions between Bulgaria and Greece also provide many development opportunities, which always include tourism. The two countries have long since discussed ideas for cooperation and for coming out with a joint tourist product. At a meeting in September, representatives of the Municipality of Gotse Delchev and the border checkpoint in Drama decided to develop a joint tourist product within PHARE's Tourist Kaleidoscope.

According to CED, the basic tasks in this field include:

- Preparing a National Tourism Development Strategy;
- Passing the Black Sea Coast Act which could curb uncontrollable and unregulated construction in the big resorts;
- Targeted solving of infrastructure problems in major tourist centers;
- Solving the problems concerning the shortage and deteriorating quality of labor in tourism, which have become visible this year;
- Intensifying the marketing and advertising of Bulgaria as a tourist destination.

Heavy summer rains and floods damaged the crop in many regions. They hit most the production of fruit and vegetables, vines and perennial plants. Overall, while damages will not have serious effect on the market, they will create problems for the processing enterprises. The data from the completed census of farms provides a clear picture of the real situation in the sector. Land fragmentation and the small size of farms are major sector characteristics. Only in the grain sub-sector, production is concentrated in larger companies and tenants, as well as in well-functioning cooperatives, which can achieve higher productivity. In the other sectors, there is an urgent need of farm consolidation and set up of functioning producer's organizations with a view to utilize the money from European funds. The new leadership of the Ministry of Agriculture and Forestry has declared the set up of Paying and Intervention Agency (based on State Fund Agriculture) and of an Integrated Administration and Control System to manage the money from European funds after 2007 its key priority. Financing from State Fund Agriculture has intensified, as well; higher attention is paid to farmers training and to the provision of information, consultations and technological assistance. Development of land relations and consolidation are also among ministry's declared priorities. The objective is to accelerate the preparation for Bulgaria's accession to the EU, gradually redirecting efforts from national to regional and farm level.

Share in GDP and GVA

Traditionally, the third quarter of the year is a strong period for agriculture, but in 2005 it was a time of disasters, which had negative effect on agricultural production. At the same time, industry and services register accelerated growth which decreases the share of agriculture in GDP and GVA. In the second quarter, this share went down 1.7 and 2.1 percentage points respectively against the same period of 2004 and for the first half of 2005 the decrease is respectively 1.3 and 1.5 percentage points. Based on current data for sector development and on recent years trends, we can project for the share of agriculture in GDP to decrease to 12.5-13 per cent in the third quarter (against 14.6 per cent in 2004), and its share in GVA – to 14.5-15 per cent (against 16.6 per cent in the same period of last year). Thus, for the first nine months of 2005 the share of agriculture in GDP is estimated at maximum 8.5 per cent of GDP and 9.5 per cent of total GVA.

Condition of the Crop

Despite the extremely bad weather and the damages suffered by the *grain sector,* achieved yields stand at about 3.4 m tons, which will be enough to secure the national grain balance. This means, that domestic consumption will be satisfied and prices will be at about the projected BGN 160/ton, VAT excluded, or close to world market levels. While yield quantities are good, the quality is not very high, which means that the production will be realized mainly as fodder grain. Exports of wheat are projected at 800 – 1 m tons, however at lower prices. The 350 thousand tons quota for duty free export to the EU has been fulfilled. In some regions the sunflower crop was damaged as well and yields are lower against last year, but, overall, they stand at good levels. The year proved particularly favorable for corn which can offset wheat and barley losses and prevent market shortage.

Heavy rains destroyed or damaged some of the *vineyard areas* in North Bulgaria. Moisture and mud blocked the necessary land treatment measures and in the most affected regions vineyard areas were hit by diseases. At the same time, in some South Bulgarian regions yields are higher compared to last year. Overall, grape crop is weak and of inferior quality. Wine grape production stands at about 350 thousand tons, or down 10 per cent on last year, and is too low (in terms of both quantity and quality) to satisfy the needs of wine producers. Bad weather conditions increased cost value (because of a need to intensify spraying) and, consequently, purchase prices which went up 15-20 per cent on last year levels. The new vineyard areas of some 22 thousand decares, which wine cellars developed with finance from SAPARD, are not yet producing crops. Hence, increase in imports can be projected.

Similar is the situation in *fruit and vegetables* production. Some part of the crop is destroyed, other is of inferior quality. While the domestic market demand may be satisfied, the processing industry will experience shortage of raw product. The production capacities of most processing enterprises rely on just in time supply of quality raw product, which means that processors will resort to import. This will confirm the strong upward trend in the import of fruit and vegetables, observed in recent years, which is a result of bad weather conditions as well as of the high cost value of national production.

Land Market

The sustainable development of agriculture improves the demand of agricultural land. The emerging special investment purpose companies contribute to land market development since most of them focus on buying farm land. Three such companies have been registered: Elana Farm Land Fund, Advance Terrafund, and Bulland Investments, with total purchased land over 9000 decares. The high market supply allows for selecting land parcels according to certain quality and size criteria (over 10 decares). The average purchase price per decare is BGN 150 – 155. Consolidated land allows for leasing at higher prices and achieving higher yield, which, in turn increases the price of Bulgarian farm land.

According to data from the National Center for Agrarian Sciences at MAF, 77 per cent of farm land is currently processed on tenant farming basis. The intervention of investment companies, which purchase land from owners for the purposes of consolidation and agricultural leasing, will increase this share. That will promote the development of large-scale agricultural production and will improve sector's productivity. The future EU accession and the opportunity to benefit from sizable amounts of subsidies will make this type of investments increasingly popular. Overall, the intervention of investment companies in the market will undoubtedly lead to much higher prices and development of a real land market.

Towards Fulfillment of Undertaken Commitments to the EU

In early September, CoM approved the report on the fulfillment of Bulgaria's commitments to the EU for agriculture. The focus is placed on the achieved progress in building a Paying and Intervention Agency and an Integrated Administration and Control System, as well as on the changes implemented in some sub-sectors.

Integrated Administration and Control System. The objective is to support the implementation of direct payment schemes by identifying every farmer applying for assistance. System's implementation will guarantee correct payments and will prevent irregularities. Building an integrated system involves creating databases of controllable parcels and carrying out control. A map of parcels will be created by means of digital ortho-photo surveys. The parcels declared by farm land owners and tenants will be plotted on the map. The maps will form the basis of the Land Parcels Identification System and will give occasion to the direct payments to farmers after 2007. Thus, only farmers who have registered their parcels and have them mapped will be eligible for grants.

Veterinary Activity. In response to the criticism for delay in the pre-accession process, the National Assembly passed on first reading a veterinary activity bill, transposing EU requirements for the production of, transport and trade in animals and products and food of animal origin. The role of veterinary doctors and the responsibility of producers are increased. The requirement to license enterprises for export is eliminated because any enterprise satisfying the veterinary and sanitary requirements will be eligible to export.

Grain Sector. NA passed an Act on the Storage and Trade in Grain, towards harmonization of grain market intervention regulations. Market intervention has been removed from the functions of the State Reserve and War-Time Supplies Agency. Ordinance on the control and accounting procedure for warehouses storing agricultural products bought through intervention has been passed. The standard contract, which State Fund Agriculture will sign with selected warehouses, has been approved. The new Intervention Agency is expected to start buying grain next year. By that time, the grain warehouses must be appointed and must have taken the necessary steps to satisfy all requirements.

Milk Sector. A National Milk Board and three regional boards (in Sliven, Dobrich and Pleven) have been registered pursuant to the passed last year Animal Breeding Act, towards implementing milk quotas at central, regional and municipal level. Boards have the task to regulate milk product prices and producer-trader relations, to control the distribution of the quotas negotiated with the EU, and the subsidies thereunder, among producers, processors and traders.

Wine and Alcoholic Beverages Sector. Measures towards sector alignment with EU requirements are focused on approving Ordinance on Vineyard Register, authorizing the registration of designated region and quality wines, and improving the qualification of sector experts. The objective is to improve management and control, to reflect latest amendments to the Act on Wine and Alcoholic Beverages and to achieve harmonization with European legislation. The register is created and maintained by the Executive Agency on Vine and Wine and allows for exercising the right to plant new and replant old vineyards. The Agency will control production capacity management and adherence to enological practices, as well as the development of the Bulgarian quality wines system. Two analysis laboratories for quality wines with appellation of origin and wines for export to the Community have been set up at the Agency.

Registration of Agricultural Producers. To benefit from direct payments for support measures under Community's Common Agricultural Policy, farmers must register their farms. Despite the extended period, a negligible portion of the existing farms have taken steps for registration. The reason is in parceled farms and the lack of confidence in the benefits of registration. According to latest data from MAF, farms total 770 thousand, with average arable land of 44 decares each. Almost 60 per cent of farms have up to 3 decares of land and may well be excluded from eligibility to subsidies. That will depend on the real calculations of the level of coverage of farmer's expenditures for social security payments and registration from the subsidy and of how much the service of such small farms will cost to the Government. If the support to small farms proves economically ineffective, that will affect most the production of fruit and vegetables. The lack of efficient producer's organizations in these sectors is also a barrier to the utilization of money from European funds and the protection of the interests of individual producers in terms of quality, prices and markets. All that is an obstacle to the voluntary registration of farmers and may call for a need of official registration.

State Fund Agriculture

Total support for autumn wheat sowing will amount to BGN 43 m, including grant aid of BGN 15.6 m. Funds are extended for purchase of quality seeds and fertilizers, to partially compensate the cost of the upswing of fuel prices, and to restrict the effects of bad weather on the grain market. The Fund has also lowered the interest rate on loans for purchase of seeds from 3 to 1.5 per cent. Lower rates, which facilitate financing, are also aimed at supporting the autumn campaign.

SAPARD

The European Commission decided to increase funding within Annual Financing Agreement 2004 under SAPARD by EUR 450 thousand. Thus financial aid under the agreement totaled EUR 68 010 thousand. Funding has been increased in response to Bulgaria's reasoned need of bigger financial resources to support implementation of undertaken commitments with respect to agriculture and rural development. Granted was also country's request for changes in two SAPARD measures – sub-measure Production of Milk and Dairy Products within measure 1, Investments in Farms, and sub-measure Wholesale Markets within measure 2, Improving the Processing and Marketing of Agricultural and Fishery Products. The first change will allow animal breeders to apply for financing under the program without having to prove that they have fodder crop areas. This will allow some 11 thousand farms, which have animals but do not have measure-required land, to benefit from the program. The second change concerns the requirement to guarantee supplies by signing contracts with registered producers. It envisages for projects based on such contracts to be attributed additional points and be considered with priority. This is believed to be an indirect incentive for the producers market and not only for the wholesale market.

Active work has started on SAPARD measure 09 Vocational Training Improvement. By regulation, there are two types of training courses: long-term (more than 150 training hours) and mid-term (30 hours). Twenty-five free courses for over 400 registered agricultural producers (owners or persons employed by registered producers under employment contracts) were organized in early August. The deadline for submission of training improvement applications by agricultural producers is 15 November and training will continue till end of 2006. This measure remains rather underused, but enjoys increasing interest.

Loans to Agricultural Producers

Banks have intensified work on extending target loans to agricultural producers. Loans are extended towards implementation of investment projects within the three programs of SF Agriculture – Animal Breeding, Plant Growing and Agricultural Equipment. A Fund-approved project and a Support Contract with the Fund are required for a loan. The fund specifies loan terms and grace periods which depend on the object of crediting. Annual interest rate is up to 9 per cent, in the form of a subsidy from SF Agriculture. In fact, this makes loans extended via the fund non-interest bearing. Besides, many banks extend special credit lines for agricultural producers beside SF Agriculture. After Reiffeisenbank, TB Allianzbank has also started such credit line. Banks also extend loans for participation in SAPARD, requiring 20 per cent borrower's participation, and 50 per cent of the financial aid from the program to go for repayment of the extended loan. Grain producers and traders are offered a special product – loan against warehouse receipts.

According to CED, special focus should be placed on:

- Mobilizing efforts to successfully complete the SAPARD Program until it is terminated upon Bulgaria's accession to the EU;
- Building the necessary institutional infrastructure, organization and capacity to manage the money from the structural funds after 2007.

*Several important events related to regional policy took place during the review period: the approval of **measures** by the European Integration Council on Bulgaria's preparation for **absorption of Structural funds** and the presentation of **draft Regional Development Plans** (at the planning regions level).*

Strategic, programmatic and planning documents

Measures to prepare Bulgaria for Structural Funds absorption

In September, the European Integration Council discussed Bulgaria's preparation for absorption of Structural Funds and the EU Cohesion Fund. The key strategic and planning documents forming the framework of fund absorption, were presented. These are the National Development Plan (NDP), its operational programmes with socio-economic and SWOT analysis. The process of implementing extended decentralisation was also discussed, as well as issues related to institutional and administrative capacity building for absorption of funds (establishment of link units for operational programs).

There is major focus on improving the training of human resource to work with Structural Funds, and the targeted training of central and local administration officials. Working rules of procedures for the relevant administrative units are also being drafted.

The so called extended decentralisation is gaining major prominence. This means that the European Commission Delegation to Bulgaria will gradually withdraw from preliminary control functions on the preparation and implementation of projects and the responsibility will be transferred to national agencies. The goal is to simplify the procedures of applying for projects. These agencies are the PHARE, ISPA, and SAPARD Executive Agencies.

As part of administrative capacity building, it is planned to assign 28 experts in planning region centres – Vidin, Rousse, Varna, Sofia, Plovdiv, Bourgas. They will work as link units for the decentralised implementation of the Regional Development Operational Programme, which is finances by the European Regional Development Fund. The establishment of regional units is also related to improving the country's administrative capacity for absorption of resources under the EU Structural Funds and the Cohesion Fund, and also in implementation of Bulgaria's commitments under Chapter 21, "Regional Policy and Coordination of Structural Instruments".

Regional development plans

Work on the preparation of new planning and strategic documents for absorption of EU Structural Funds continues. In parallel with the drafting of the NDP and its 6 Operational programmes there is also a process of preparation of ***Regional Development Plans***.

The drafts of Regional Development Plans for the 2007-2013 period are now ready. The Ministry of Regional Development and Public Works is in charge of coordinating the preparation of these plans written in line with the requirements of Art. 11 of the Regional Development Act.

The documents contain detailed and in-depth analyses of the planning regions' economic, social and environmental development.

An important aspect in these plans is the establishment of ***a medium-term strategic framework*** for the development of the 6 regions including goals, priorities and measures. When setting the strategic goals, the authors took into consideration both the regions' specifics and the overall long-term framework of regional policy as defined in the National Regional Development Strategy of Bulgaria for 2007-2015. The Regional Development Plans will be the foundation of the National Operational Programme for Regional Development.

The technology of preparation and efficient implementation of plans requires extensive public support. That is why the process of developing these plans is based on ***public-private partnership***. The draft plans are available on the Ministry of Regional Development and Public Works website and are the subject of a wide discussion; all opinions and comments will be taken under consideration at the finalisation of plans..

Raising the awareness level of local authorities, businesses and citizens on the goals of regional policy and the opportunities created by Structural Funds will be discussed in a series of seminars, organised in September and October by the European Commission's Delegation in Sofia. Commission experts have defined the fundamental issues in drafting and implementing regional policy as follows:

- limited exchange of information;
- lack of knowledge; experience and motivation impeding the process of forming regional policy.

To address these issues, during workshops held in the 6 planning regions the subject of discussion was their own development potential and the role to be played by European funds.

Priorities in absorption of resources under Structural Funds

The resources from EU Structural Funds, amounting to EUR 2.3 b, will be used in several major aspects: 1) to improve regional infrastructure (roads, Water and Sewerage systems, environment at local level); 2) development of human resources, strengthening administrative capacity and staff training; 3) improving the competitiveness of economy and, above all, of SMEs. Infrastructure will be a top priority because it is among the country's key problems impeding the successful development of business and economy.

The experience gained so far by Ireland, Portugal and Spain in using Structural Fund resources, is of particular interest. For instance Ireland made its top priority improving the quality of human resources.

And all three countries the effects of funding are manifested in several different ways:

- boosting entrepreneurial activities;
- modernisation of the productive base (increased production capacity);
- support to companies in introducing new technology;
- improved quality of human resources, job creation and lower unemployment;
- improved level of education and training of the workforce;
- improving infrastructure;
- opening up of the economy – effects on trade and foreign investments;
- rational and efficient use of transfers by establishing institutional and financial capacity, establishment of public-private partnerships.

Municipal finance and the fiscal decentralisation process

Issues related to forming municipal budgets and financial decentralisation gained particular prominence over the past months. This was triggered also by the natural disasters that hit a number of regions in the country.

The National Association of the Municipalities in Republic of Bulgaria (NAMRB) made its demands to the government when discussing Budget 2006. A major item of discussion was the proposal on increasing the subsidy for capital expenditure on municipal infrastructure and provide separate resources for overcoming the effect of natural disasters in 2005, as well as resources for prevention of local sites. In connection with this, the NAMRM will insist that the State Budget Act for 2006 should provide resources ***to set up a Disaster and Emergency Relief Fund*** at each municipality; this money is to be used for immediate response to crisis situations.

Another important aspect in proposals is the mayors' idea to increase municipalities' tax revenues by updating the tax base of immovable property according to market prices. Particular attention should be given to implementing financial decentralisation as it requires legislative changes in local government. This concerns the drafting and adoption of the ***Local Finance Act*** regulating in a new way payments from the national budget of public services provided by municipalities. This new legislation should also regulate the efficient and transparent management of taxpayers' money, and the relationship between local and central government budget.

Efficient financial decentralisation requires a stable revenue base for municipalities This can be achieved in several ways: by increasing the size and scope of local tax when re-distributing the tax burden; by transforming personal income tax into a local tax; by introducing municipal VAT or turnover tax. These are some of the NAMRB proposals on forming municipal finance.

The Association also insists on the adoption of the amendments to the Constitution submitted to the previous National Assembly; these changes would enable mayors to establish the type and size of local tax and charges; another proposal was that a new financial decentralisation programme should be discussed and adopted.

Good practices in local government

Public-Private partnerships

A number of good practices are being implemented in local government. The focus is increasingly on developing public-private partnerships when drafting strategic and planning documents for municipalities. A good example would be the preparation of the municipal development plan for 2007-2013 period in ***Dobrich Municipality***.

Local authorities and the business community are working in cooperation through a dedicated municipal unit responsible for work with investors. Its goals are: the preparation of a programme in support of the development of existing enterprises in the region, developing a marketing strategy for the region which includes providing fast and comprehensive information to potential investors. Of particular significance are the Labour Force Profile Analysis and the proposed measures for staff training and re-qualification in compliance with entrepreneurs' requirements and needs. An Investor Promotion Programme is currently being developed; it will provide for preferential treatment: discounts on lease paid for municipal sites. The design of a new industrial park is now ready; it is expected to be funded under the PHARE Programme.

A number of municipalities have set up ***Advisory Committees*** to ensure the direct involvement the local business community in decisions related to the region's future development.

The Foundation for Local Government Reform is currently implementing a project entitled "Marketing of Bulgarian Municipalities and Local Economic Development" supported by the United States Agency for International Development (USAID). The purpose is to promote partnership between businesses and local authorities in improving the business environment. As part of the project, 8 municipalities were given special Business Development certificates. These are the municipalities of Dobrich, Silistra, Gabrovo, Montana, Pleven, Razgrad, Stara Zagora and Haskovo. An assessment of municipalities' capacity to efficiently apply good practices and introduce successful governance models was performed. The assessment criteria on municipalities' preparedness to work with businesses include: establishing a labour force development programme; participation by businesses in important decision-making processes by the municipality through Advisory Committees, developing detailed information on available buildings and sites; establishing an Industrial Profile of the municipality.

Local government cooperation in South East Europe

Local government cooperation in the region is very important to the exchange of good practices and experience useful in local economic development

NAMRB is one of the founding members of the Federation of Local Government Associations in South East Europe founded in 2001 on initiative by the Bulgarian Association. The association was institutionalised last year. In September 2005, the NAMRB Executive Director was elected its president. This is clearly a gesture of recognition for the Bulgarian association's active work.

The role of the association is positively evaluated as it contributes towards strengthening cooperation in the region and the exchange of experience. The international network's goals include: contribute towards deepening and strengthening of the processes of decentralisation and democratisation in the region governed by the principles of the European Charter of Local Self-Government; enhance and streamline the exchange of information and experience between local authorities; strengthen the positions, authority and capacity of each member association. Another important goal of the network is to promote the development of joint projects and the joint presentation to potential donors. And last but not least, the Federation's importance in promoting technical twinning should be mentioned.

Necessary steps in this area according to CED:

- stepping up the process of preparation of planning and strategic documents for the absorption of resources under the Structural Funds and EU Cohesion Fund;
- conducting active awareness-raising policy among the business community and civil society on the challenges and opportunities of accession and structural funds;
- adopting measures to increase the institutional capacity of central and local administrations in EU funds absorption.

In the first months after its constitution, the National Assembly focused its work on passing of a number of procedural instruments on its structure and activity[29] and on the activity of parliamentary commissions. In this short period, the Parliament and the Cabinet passed few pieces of economic legislation, leaving for October the discussion and approval of the most important ones and of key instruments for Bulgaria's EU accession, like the new Criminal Procedure Code[30].

Commercial Act

Commercial Act[31] amendments are the most important revision of existing economic legislation. The dynamics of Bulgarian market relations in recent years and country's future accession to the European Union have made it necessary to improve and align some provisions of the Commercial Act and of related legislation with European and international standards[32].

The general section of the Commercial Act was amended and supplemented in line with: First Council Directive 68/151/EEC on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, with a view to making such safeguards equivalent throughout the Community; Second Council Directive 77/91/EEC on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with a view to making such safeguards equivalent, and Eleventh Council Directive 89/666/EEC concerning disclosure requirements in respect of branches opened in a Member State by certain types of companies governed by the law of another State. These amendments and supplements to the Commercial Act were aimed at aligning Bulgarian company law with Community law. In line with the above directives, amendments were made in three company law areas: commercial law **publicity, validity of actions** of company bodies with respect to third persons, and **nullity** of companies.

Regarding the **validity of actions** of company bodies with respect to third persons, a provision has been adopted to the effect that registrable facts are disclosed on behalf of a trader **by a person or persons who legally represent such trader**.

In the event of change of bodies or representation, the new body or representative files an application for registration of this amendment. Amendments and supplements to limited liability company regulations specify that authorization, or deletion thereof, has effect with respect to third persons acting in good faith **upon registration of such authorization or deletion thereof.**

Regarding the nullity of an incorporated company, the rule that the court decision declaring nullity of the company produces effect upon its entry into force (in other words, it is not retroactive) has been preserved. Termination is entered ex officio in the commercial register, whereupon liquidation is started. According to the latest amendments and supplements, the notice for termination is promulgated in the Official Gazette when there had been a requirement for promulgation of company's incorporation.

Hence, regarding the publicity of facts in the company's case, a rule has been introduced to the effect that before the expiry of 15 days after the publication, disclosed facts shall not be relied on as against third parties who prove that it was impossible for them to have had knowledge thereof.

Regarding traders' obligation to include in their business correspondence certain individualizing particulars like company name, seat, and other, it has been specified, that when a commercial company discloses the amount of its capital, it shall also disclose the amount of capital subscribed for and paid up. In that connection, regarding the compulsory disclosure in the instrument of constitution of a joint-stock company of the amount of capital, a requirement has been included for disclosure also of that portion of the subscribed capital, which has actually been paid up upon company's constitution. Annual financial reports of companies (until latest amendments – annual accounting reports) always give information about the number and nominal value of the shares of a company acquired and transferred by the company itself over the year; after the amendments, they will also specify the portion of the capital, which the shares represent, as well as the price of their acquisition or transfer.

The second group of amendments regulates the maintenance and change of the capital of joint stock companies for the purpose of protecting and safeguarding the interests of shareholders and third persons.

In that connection, latest amendments prohibit for the shares of a company to be subscribed for by the company itself. If shares are subscribed for at company's constitution in contravention to this prohibition, the founders are jointly liable for the payments against the shares subscribed. If the shares of a company have been subscribed for by a person acting in his own name, but on the account of the company, the subscriber shall be deemed to have subscribed for them on his own account. Companies may acquire their own shares only in special circumstances

29 Rules on the Structure and Activities of the National Assembly, prom., OG, No. 69 / 23 August 2005, in effect since 23 August 2005, amm. and suppl., No. 74 / 13 September 2005.

30 To date, the National Assembly has not passed yet on second reading the new CPC; MPs make efforts to pass the Code by 7 October with a view to include it in Bulgaria's achievements in the European Commission monitoring report on Bulgaria's progress towards EU accession. However, most likely this term will not be observed and the Code will be passed about 15 October 2005.

31 By the Act on Amendments to the Commercial Act, promulgated in Official Gazette, number 58 of 27th of June, am. Number 66 of 12th of August 2005.

32 STATEMENTS to the Bill Amending and Supplementing the Commercial Act (№ 502-01-26 / 15 April 2005).

like reduction of capital, universal succession, other than transformation and some other cases provided by law. The amendments and supplements introduce a compulsory requirement for shares to be fully paid up in most of the cases, in which companies acquire their own shares.

The third group of amendments concerns the registration of branches of foreign commercial companies on the territory of the Republic of Bulgaria. They regulate the relations concerning entry of branches of foreign companies in the commercial registers, disclosure of the particulars of the application for entry, documents accompanying the application for registration of a branch. Overall, this is a new subject matter in Bulgarian commercial law. It has an analogue only in the Act on Non-Profit Legal Persons with respect to branches of foreign non-profit legal persons33.

Amendments introduce new rules regarding the regulation of the transformation of commercial companies, which are aimed at facilitating the procedures for sole-proprietor commercial companies.

Public Offering of Securities

Two pieces of legislation concerning the subject matter of public offering of securities have been passed – Rules on the Structure and Activities of the Fund for Compensation of Investors in Securities[34] and Ordinance No. 22 / 29 July 2005 on the terms and procedure of entry in and deletion from the register of the Financial Supervision Commission of public companies, other issuers of securities and securities issues[35].

According to the Rules on the Structure and Activities of the Fund for Compensation of Investors in Securities, the Fund is a self-supporting legal person, managed and represented by a management board. The Fund's management board specifies the percentage of the annual payment due by investment intermediaries, including foreign investment intermediaries who provide additional compensation to their clients in Bulgaria. The management board promulgates its decision in the Official Gazette and publishes it in its site by 31 December of the previous year. The Fund has been set up on basis of the latest amendments to the Act on Public Offering of Securities (APOS) aimed at aligning Bulgarian legislation with Directive 97/9/EU concerning **investor compensation** schemes. A major function of the Fund is to provide compensation to the clients of investment intermediaries when the latter are unable to fulfill their obligations towards clients, particularly when the investment intermediary is in a procedure of bankruptcy, or a competent supervisory body has established that it cannot fulfill its obligations towards its clients. The Fund raises money from affiliation fees from investment intermediaries, annual installments from investment intermediaries; income from investment of accumulated assets; refunds from investment intermediaries in cases where the Fund, upon payment of compensation to a client, has entered into the rights of such client in respect of the investment intermediary; from interest on outstanding claims, and from other sources. The annual payment by foreign investment intermediaries who provide additional compensation to their clients in Bulgaria is calculated as a percentage of total client assets in Bulgaria, pro rata of the additional compensation provided by the Fund.

The second passed piece of legislation concerning the subject matter of public offering of securities – Ordinance No. 22 / 29 July 2005[36], regulates the terms and procedure of entry in and deletion from the register maintained by the Financial Supervision Commission of public companies, other issuers of securities, and securities issues. According to the ordinance, any person who **either**:

1. has a prospectus for initial public offering of securities according to the Act on Public Offering of Securities (APOS), confirmed by the Commission;
2. has a prospectus for secondary public offering of securities;
3. has a prospectus for initial or secondary public offering of securities according to Article 141 of APOS;
4. is not required to publish a prospectus for initial or secondary public offering of securities in the cases referred to in Art. 79 of APOS, where all other conditions of the act are met; or
5. is released, upon a decision of the Commission, from the obligation to publish a prospectus for initial or secondary public offering of securities according to Art. 88 of APOS,

shall be entered in the register as **issuer of** securities**.**

A shareholding company, which, according to the terms and procedure of the Ordinance, has been entered in the register **as a public company, shall not be entered as issuer.** If the shares for initial public offering are to be subscribed for at the constituent meeting of a shareholding company, such company shall be entered in the register as issuer under incorporation.
According to the Ordinance, any:

1. issuer of shares, who has become a public company on basis of entry of the act of its constitution or of the increase in its capital in the commercial register;
2. shareholding company, including when it is entered in the register as issuer of an issue of shares for secondary public offering which satisfies certain specified conditions;
3. shareholding company, including when it is entered in the register as issuer, in case where it has become a public company, has on the last day of two consecutive calendar

33 Shorthand record of discussions on the draft Act amending and supplementing the Commercial Code (No 554-01-6 / 21 January 2005, XL National Assembly).

34 By decision No 40-P / 10 August 2005 of FSC, prom., OG, No. 69 / 23 August 2005.

35 Adopted by Decision No. 39-N / 29 July 2005 of the financial Supervision Commission, prom., OG, No. 66 / 12 August 2005.

36 Adopted by Decision No. 39-N of 29 July 2005 of the Financial Supervision Commission, prom., OG, No. 66 / 12 August 2005.

years more than 10 000 shareholders, and provided that its issue of shares satisfies certain specified conditions,

is entered in the register as a **public company.**

Any **newly incorporated and successor company or companies,** which have become **public as a result of transformation** involving a public company, are entered in the register as **public companies**.

According to the Ordinance, in some cases the entry of an issuer is initiated by the Commission and in other – by the company. Where entry is initiated by the Commission, the latter enters the issuer in the register upon deciding on the confirmation or approval of a prospectus or on exemption from the obligation to publish a prospectus, as the case may be. The Commission notifies the person in writing, within seven days after the decision for entry. In cases where publication of a prospectus is not required, entry of an issuer in the register is initiated by the company, which issues or has issued the securities, by the offerer of securities, or by the person who wants for the securities, of which he is not issuer, to be accepted for trade on regulated markets. The person files an application for entry of the company, which issues or has issued the securities, as issuer, within 7 days from the date on which the competent company body according to its statutes has taken a decision for public offering of securities issue.

The ordinance regulates also the terms and procedure of striking off the register public companies, other issuers of securities and securities issues.

Technical Requirements to Products

Latest amendments and supplements to the Act on Technical Requirements to Products promulgated in OG, No. 43 / 20 May 2005, called for adopting of Ordinance on Conformity Marking[37]. The Ordinance regulates the rules of placing and the graphic image of the conformity mark. The conformity mark certifies that the products comply with the requirements applicable to them as set forth in the implementing instruments of the Act on Technical Requirements to Products and that they have passed through the respective conformity assessment procedures. When a product falls under the provisions of more than one ordinance, each of which envisages placing of a conformity mark, the marking shall certify product's conformity with the requirements of each one of the ordinances. The producers, or such other persons as may be specified in the ordinance, must place the conformity mark on the products before they are marketed and/or put into operation. The conformity mark consists of the initial **"CO"** with graphic image according to Annex No. 1 to the Ordinance. When the Republic of Bulgaria is a party to effective agreements for mutual recognition of conformity assessment results and acceptance of industrial products, signed with the European Communities and their Member States, or with the member countries of the European Economic Area/European Free Trade Association (EFTA), the conformity mark of products falling within the scope of such agreements will consists of the initial "CE" with graphic image according to Annex No. 2 to the Ordinance. From the date on which the agreement for Republic of Bulgaria's accession to the European Union takes effect, the conformity mark will consist of the initial "CE" with graphic image according to Annex No. 2 to the Ordinance.

The conformity mark is placed on the product or on its data plate and if that is not possible, the conformity marking is placed on the packing and on the documents accompanying the product, where such documents are required under the respective ordinance. Products with marking according to the repealed Ordinance on Marking for Conformity with Essential Technical Requirements to Products are deemed to comply with the requirements of this ordinance. Products, marketed and/or put into operation with placed conformity mark "CO", which fall under the scope of the agreements for mutual recognition of conformity assessment results and acceptance of industrial products mentioned above, are deemed to comply with ordinance requirements until available quantities become exhausted, but in any event for no more than one year after the above agreements take effect.

RULES on the Implementation of the Public Procurement Act

According to the latest amendments to the Rules on the Implementation of the Public Procurement Act[38], public procurement assignors, which are public legal entities within the meaning of PPA, Additional Provision, § 1, item 1, can award public procurement contracts under facilitated conditions envisaged for sector contracting authorities, but only when they carry out utility sector activities like water supply, electricity, transport, postal services. Assignors, which are public legal entities, have the right to select the type of procedure under PPA for award of the specific contract. There are some restrictions only for the negotiation procedure without notice. When carrying out any other activities, assignors, which are public legal entities, shall not have the right to enjoy the preferences for sector assignors. This amendment is in line with Directive 93/38/EU.

The adopted amendments to other provisions of the Rules result from the amendments to the Official Gazette Act of 1 May 2005[39], which stipulate that notices under PPA shall

37 By DCM No. 191 / 16 August 2005, prom., OG, No. 69 / 23 August 2005.

38 Adopted by DCM No. 250 / 17 September 2004, prom., OG, No. 84 / 27 September 2004, in effect since 1 October 2004, corr., No. 93 / 19 October 2004, amm. and suppl., No. 59 / 19 July 2005, in effect since 19 July 2005.

39 According to the amendments to the Official Gazette Act, promulgated in OG, No. 31 / 2005, since 1 May 2005 public procurement notices Public Procurement Act will be published in the Official Gazette site at http://dv.parliament.bg/.

be published in the Official Gazette site **in electronic form –** magnetic medium or e-mail. The requirement for sending notices on paper carrier was revoked.

ORDINANCE on Awarding Small Public Procurement Contracts

Latest amendments to the Ordinance on Awarding Small Public Procurement Contracts[40] are in line with the amendments to the Official Gazette Act. They envisage for notices to be sent simultaneously to the Official Gazette for publication in its site and to the Agency for entry in the Public Procurement Register. Notices are published in the Official Gazette site within 5 days after they are sent.

Based on the brief review of the legislation activity of the National Assembly and the bodies of the Executive, we can draw the conclusion that there are no any essential amendments and supplements to economic laws. A couple of important pieces of legislation, including the Insurance Code, are pending for adoption in the next months. The Council of Ministers approved the draft Insurance Code on 15 September 2005 and it is under discussion in the parliamentary Budget and Finance Commission. By passing the Insurance Code, Bulgaria will fulfill its commitments for aligning national insurance legislation with EU directives.

40 Adopted by DCM No. 249 / 17 September 2004, prom., OG, No. 84 / 27 September 2004, in effect since 1 October 2004, corr., No. 93 / 19 October 2004, amm. and suppl., No. 59 / 19 July 2005, in effect since 19 July 2005.

INFLATION AND CREDIT – ANALYSES AND PROGNOSES

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Introduction

Inflation is a basic macroeconomic indicator. We offer a series of five sections where inflation and credit are discussed on basis of a strict economic analysis.

- Section One examines the fundamentals of inflation.
- Section Two provides analysis of and prognosis for the development of inflation in the USA.
- Section Three provides analysis of and prognosis for the development of inflation in Bulgaria.
- Section Four studies the role of credit in the inflationary process.
- Section Five substantiates the need for drastic measures to restrict bank lending in Bulgaria and proves the detrimental consequences of its tremendous growth.

Fundamentals

The economic literature abounds in theories offering plenty of classifications. Surprisingly, however, even monetarists do not have any sound inflation analysis system and confine themselves to the domain of monetary policy. Only the Austrian school provides a valid theory, which history has proved to be reliable. Therefore, we follow this theory in our presentation, citing its classical scholars Ludwig von Mises and Murray Rothbard.

The general understanding of inflation as total increase of prices is fundamentally flawed. The correct definition of inflation is "growth in the supply of money". In other words, the increase of money and bank credit is called inflation. Rising prices are a result of inflation. The correct approach of determining whether the inflation is "low" or "high" is to compare the supply of money to prices, in other words, money supply growth to price increases. This will be illustrated best by an analysis of inflation in the USA and in Bulgaria.

We identify three phases of the inflationary process. For simplicity of terminology, we logically call them (1) low inflation, (2) high inflation, and (3) hyperinflation. Let us discuss in detail these phases.

Phase One – Low Inflation

It is impossible to define inflation as low or high in quantitative terms. The only definition that makes sense is the one in qualitative terms. We define inflation as "low" when general price increases are lower than money supply growth. In other words, while money supply increases, aggregate price level growth remains slower. Hence, some economists call it "hidden" inflation – there is inflation, but it is not visible. The explanation is simple: when money supply begins to increase, consumer prices do not go up immediately, but with some latency, which can reach one or two years.

There are two reasons for that. First, as people believe that the rise in prices is temporary and later prices will normalize, they spend less of the newly earned money and keep more money with them, whether in cash or on deposit. In short, money demand increases. Second, as people have more money on hand, instead of spending it or keeping it on savings deposits, part of the newly generated money is "invested" in the securities, bond and real estate markets. Hence, the prices of investment assets increase. This growth is wrongfully perceived as "bull" market, and not as inflation.

Besides, incomes increase faster than prices, which means that the real purchasing power of people, businesses and the Government improves. Increasing real incomes combined with rising asset prices create an illusion of economic growth and prosperity. Economic activity accelerates and the economy goes through the illusionary phase of economic boom. Optimists call such inflation "good", journalists – "favorable", doctors – "benign", politicians – "harmless", bankers – "controllable", and for Austrian school disciples, it is the inevitable prelude to even more inflation.

We shall now highlight the key point, essential for the understanding of this inflation phase: as the Government derives income from the growing money supply and since the increase of prices is slower than the increase of Government's income, the Government actually improves its real purchasing power. To put it in plain language, the Government is financed by money printing. Such income is known in the popular literature as "inflation tax" and in the specialized literature – as "seigniorage". Hence, while inflation is low, the Government profits from it and will continue to increase money supply, in other words, to print money and stimulate credit growth. We emphasize that credit growth actually leads to money supply growth and inflation, but we shall leave this rather complex topic for the last two sections of the series.

Phase Two – High Inflation

Unfortunately, low inflation cannot last forever. People realize eventually that the current high prices will become higher. They understand that they profit by buying "now" and begin to step up their purchases. The increase of the general price level accelerates. Consequently, the purchasing power of Government's income begins to erode. If the Government steps up "printing", consumers, in response, step up their purchases. Consumers begin to spend not only their new income, but also the money they have accumulated so far. At this point prices begin to increase faster than money supply. The economy switches to a completely new regime – that of "high" inflation.

As Rothbard points out in Man, Economy, and State, (Murray Rothbard, Man, Economy, and State), "Hyperinflation begins at this stage." To put it in economic terms, money supply growth leads to lower money demand. In this phase, inflation shows its ugly face. Now it is not "harmless" but "malicious". Prices keep on rising and incomes cannot keep up with them. The cost of living goes up. Real incomes go down and people begin to feel that they are growing poor. Interest rates reflect higher inflationary expectations and go up. Consequently, prices of securities go down and so do prices of bonds, usually accompanied by real estate prices, because higher interest rates decrease mortgage demand and, hence, home and real estate demand. The economy gets into stagnation. The general feeling of prosperity vanishes and consumers cut down their expenses. Hard times come. As inflation deteriorates, prices go up while people cut down their holding of money. As a consequence, general economic crisis develops. Shortage of available money is felt and a need for more money is universally proclaimed. In short, high inflation leads to the need for even more inflation, thus creating a vicious circle. For pessimists, high inflation is "bad", for politicians and for the budget – "malicious", for doctors – "malignant", for journalists – "unfavorable", for bankers – "uncontrollable", and for the people – "blood-sucking".

Phase Three – Hyperinflation or Deflationary Collapse

Phase Three has two alternative outcomes: (1) hyperinflation and (2) a deflationary collapse. In the first case, the situation described above becomes uncontrollable and an incompetent Government succumbs to the general pressure for more and more money. Money supply accelerates significantly, now at almost exponential pace. "Hyperinflation" begins – the third and final phase of inflation. Ludwig von Mises calls it "flight into real goods" and describes it as follows: "Everyone hastily exchanges his or her money for goods, any goods, no matter whether he or she needs them and how much he or she will have to pay for them." Rothbard calls this "flight from money" and describes it as "getting rid of money as soon as possible with a view to "invest" this money in real goods – any goods – as a store of value for the future. This mad scramble away from money, lowering the demand for money to practically zero, leads to astronomic rise of prices. The value of the monetary unit falls practically to zero … The economy collapses." Hyperinflation ruins the middle class and wipes out the fixed income groups. It ultimately leads to disastrous unemployment and distressingly lower living standards. This scenario is painfully familiar to all Bulgarians.

Deflationary collapse is the alternative scenario to hyperinflation. While control over inflation is not yet completely lost, inflation becomes so massive, painful and unbearable that a competent government is forced, though unwillingly, to stop the "printing". It is important to note that while in an environment of low inflation the Government profits from money printing, in a situation of high inflation profits quickly vanish and even become negative, because high inflation eats up the purchasing power of the whole budget. General budget's purchasing power losses become higher than incomes from newly printed money no matter how fast the Government prints money. Having no further prospects for profit and facing the real threat of losing even more, a competent Government prefers to stop the printing presses, to put an end to the false boom, so a collapse gets under way. According to Rothbard, collapse is the wiser way out than hyperinflation. Bulgarians will readily agree with him.

Careful readers have already noticed certain lack of correspondence between the terminology that classical scholars use for the different inflation phases, but we shall not dwell on this question. The reader may well expect us to apply the above understanding to two specific analyses of inflation -- in the USA (Section Two) and in Bulgaria (Section Three), while discussing in the last two sections bank credit (Section Four) and the need to restrict its expansion (Section Five).

Analysis of U.S. Inflation

Significance of Inflation

Passionate inflation-deflation debate is going on in the international financial and investment literature. Publications on whether inflation in the USA will continue or deflation will prevail are coming out every day. Today, the situation in the USA is similar to that in the late 1920s, when USA's gross accumulated debt was 300 per cent higher than the gross domestic product. Overwhelming debts in the American economy have a deflationary effect because payment of such debts decreases money supply. Let us remind that in any economy credit growth leads to money supply growth and has an inflationary effect. This ultimately leads to a general rise of prices and to currency devaluation. Conversely, debt payment leads to decrease of lending and has a deflationary effect, which results in lower prices and currency revaluation.

We fully agree with the modern titan of economic and investment analysis Jim Puplava that the most important part of the strategy of any global investor for the next decade is the correct analysis of and forecast for the development of inflation in the USA. In a deflationary environment, the correct investment strategy is cash and government bonds. Such was the situation during the Great Depression in the 1930s, when money supply decreased, prices went down and everything lost value. Home prices dropped by some 70 per cent and ruined most of the American families with mortgaged homes. In an inflationary environment, however, such investments are fatal – inflation quickly eats up without return the value of both money and bonds.

Generally, the correct investment strategies for inflationary and deflationary environments are mutually exclusive. The correct strategy for the one environment is fatal in the other, and vice versa. Hence, the correct forecast for the future inflation in the economy is vital for choosing the correct investment strategy. For Americans, the importance is obvious. For people outside the USA this is important if they have investments in the USA (shares, bonds, etc.), or if they hold US Dollars. In general, if the US Dollar were going to depreciate, it would be a good thing to know that.

Our objective is to make an analysis of and forecast for the inflation in the USA. With that end in mind, we apply the criterion for the state of inflation in the USA and take into account the current inflation phase. Finally, we make a reasoned prognosis for future inflationary trends in the USA, the appropriate investment strategy and the future of the dollar in an inflationary perspective. The Bulgarian reader will benefit from getting to understand the nature of rising home prices in the USA and in Bulgaria.

Analysis of Inflation in the USA

We remind that we distinguish three consecutive phases of the inflationary process. For simplicity, we call them: (1) low inflation, (2) high inflation, (3) hyperinflation. We define inflation as "low" when consumer price increase is slower than money supply, and as "high" when consumer prices rise faster than money supply. Hyperinflation is characterized by price upswing, fast depreciation of money and ultimately leads to collapse of the currency, which is then replaced by another currency and the inflationary cycle begins again.

Overall, in the last 12 months consumer prices in the USA went up by about 2.7 per cent. Year on year inflation for 3, 6, 9-month periods and for 1-3 year period is about 1-3 per cent. Some more aggressive inflation measures stand at about 5-7 per cent. More specifically, according to BLS data, CPI (All Urban Consumers) stood at 175.1 in January 2001 and at 185.2 in January 2004. This makes 3-year growth of 5.8 per cent at a rate of 1.9 per cent year on year.

At the same time, money supply growth measured by broad measure M3 is 7-8 per cent year on year. According to Federal Reserve data, in the above 3-year period money supply increased from US$ 7.25 b to US$ 8.9 b. Total three-year growth stands at 23 per cent, or 7.1 per cent annually.

Under these circumstances, we can conclude that in the period 2001-2004 consumer prices register slower growth (1.9 per cent) compared to money supply growth, or inflation in the USA is still low.

We need to include here some important explanatory notes. First, the period January 2001 – January 2004 was chosen for convenience of calculations and with a view to facilitate the reader. Whether the period starts a little earlier or later and whether it is a little longer or shorter has no effect on the final result. Second, there are several variants of the basket of goods index, in other words, there are several basket of goods variants, but the selection of a basket variant does not change significantly our analysis. Third, a recently published comprehensive and authoritative analysis by Peter Williams concludes that Government's basket of goods variant undervalues the increase in the real basket of goods by 2.7 per cent year on year. Even with that in mind, our basic conclusions remain valid.

Our conclusion is supported by a number of observations, particularly by statements of senior government officers, politicians, Wall Street, and financial analysts. Still more important is the lack of uneasiness in consumers about rising prices. With all things going on, consumers are not worried by the depreciating dollar on international markets. They moan about rising oil and home prices in the USA.

A close relationship between money supply growth and rising estate property prices has been observed in the USA in recent years. Of course, there is such relationship in any market economy, including Bulgaria. Given the expected depreciation of money, the USA consumer strives to invest it in assets, which do not lose value or have, at least, sustainable value. This is de facto "escape from money", which we mentioned in the previous section or, in other words, "flight to estate property". This also explains why consumer price index growth is slower than money supply, namely because a larger portion of the new money supply generated by loans is eaten up by homes and has not yet spread across all consumer goods. This is so in Bulgaria as well.

In other words, when the State depreciates money through inflation, consumers counteract by "investing" in homes. This close relationship between inflation and rising home prices is well developed in the literature on inflation. We recommend to our readers to find on the Internet (www.mises.org) the article "Weimar and Wall Street" by the inflation expert Robert Blumen. In our analysis, we have concentrated on this relationship because it applies directly to the current Bulgarian reality. Prices of Bulgarian real estate are soaring for the same reason they do so in the USA – credit inflation.

Conclusions about Inflation in the USA

Inflation in the USA is still low. Under these circumstances, consumers wisely focus on estate property before their money depreciates. Given that the Government benefits from inflation, one can expect the US Government to proceed with its inflationary policy. Drawing on history, we can expect low inflation to continue for another 2 – 4 years, followed by a high inflation phase of 3 – 5 more years. This means that the dollar will depreciate further and fall on international markets. Within the inflation-or-deflation debate, we did not argue that there would be no deflation; we maintain that there will be inflation in the USA in the next 5 – 8 years, while subsequent deflation is possible. Under these circumstances, the rational choice for investors is inflationary strategy. As we will see in the next section, this is the correct strategy for Bulgarians, as well.

Analysis of Inflation in Bulgaria

The wealth of statistics, which BNB have made available at www.bnb.bg, is commendable. From Statistics we go to Monetary Survey and download Short Monetary Survey for the period November 1999 – November 2004. Latest available data are from November 2004, hence we choose November as a starting month with a view to cover five full years.

We prefer for our analysis the measure “Broad Money” M3. It reflects best the meaning of the term Money Supply in an inflationary aspect. Scrolling through data makes it apparent that money supply growth is rather regular in time. This means that year on year growth is more or less smooth and choosing 2-, 3- or 5-year period makes no difference for the final result. In November 1999 supply stands at BGN 7.08 b and in November 2004 – at BGN 18.86 b. This means that for five years money supply went up 166 per cent, which makes 21.6 per cent growth year on year. In other words, averaged year on year inflation for the last five years is 21.6 per cent. At this point, we explain parenthetically that money supply statistics seem correct and reliable, and history shows that government institutions rarely manipulate them intentionally.

We retrieve data about the rise of consumer prices from the Macroeconomic Review report. The most representative is the CPI Average column, which gives for the years 2000-2003 values of 10.3 percent, 7.4 per cent, 5.8 per cent, 2.3 per cent, accordingly. The fact that price rise decreases year on year immediately catches our eyes. History teaches that, as a rule, consumer price data should not be taken in good faith, given that the government institutions of any state are interested in manipulating these statistics for a number of reasons. In other words, the reliability of such data is always disputable. For example, while 10.3 per cent price increase in 2000 seems plausible, no Bulgarian who pays for food and heating will agree without demur that in 2003 prices rose by only 2.3. Everybody can make alone this calculation, while it is also clear that the real value is definitely not above 21 per cent, which is of key importance to our analysis. Given the fact that average money supply growth is 21.6 per cent and the consumer prices increase is slower, we can infer that inflation in Bulgaria is low in recent years. Based on the discussion in the previous two sections, we can draw plenty of conclusions.

Recommendations and Forecasts

Given that inflation is low, the State and the Government profit from pursuing their inflationary policy. We have established that in the first section. Under these circumstances, we can draw the conclusion that inflation in Bulgaria will accelerate.

Our second conclusion is that the Bulgarian Lev will keep on losing purchasing power, in other words, it will keep on depreciating. In this situation, Bulgarians should pursue inflationary investment strategy. This means investing in real assets like homes, enterprises, stable foreign currencies with slower depreciation against the Lev. Of course, Bulgarians have long been doing that. Take for example homes. According to many real estate agencies, in 2004 growth in home prices stands at about 35-40 per cent, or much above the inflation value of 21.6 per cent. This means that homes absorb a huge portion of the newly created money and loans. In other words, inflation is most pronounced in the housing sector.

There are two basic views – investment and inflationary, on which we can base our home purchase analysis. For a couple of years now, Bulgarians think that “investing” in homes is among the best possible investments. Of course, this is very naïve and unreasonable from an investment point of view. Examination of well-documented 700-year span of data about homes in the Roman Empire reveals that this is not the case. Similarly, 500-year period of data for Great Britain and 200-year period of data for the USA clearly demonstrate the naivety of such point of view. In an inflationary perspective, however, “investing” in homes is, indeed, among the best ways for the individual to escape the extortionate currency depreciation as a result of inflation. From an inflationary point of view, buying a home is strongly valid and completely rational.

Buying a home prompted by the decreasing purchasing power of the currency could hardly be called investment and even less “good” or “sustainable” investment. In such cases, buying stable currency would be much more appropriate. By buying stable foreign currency, one preserves best his or her purchasing power, remains highly liquid and can derive income by investing in bonds denominated in that currency. Betting on home prices to increase faster than a stable foreign currency is speculative and characterizes the purchase of a home as speculation, especially when it is made with a bank loan. Speculation is an important inflation topic, which is closely related to bank loans, and we shall proceed with its analysis in the next section.

As we mentioned earlier in this paper, the production assets of enterprises provide an alternative to homes. As these are not directly sellable or buyable, the share of an enterprise is a near substitute. It embodies a share of all assets of the enterprise and, as such, it can be perfect protection against inflation. In other words, investing in the stock exchange is strictly rational from an inflation point of view. We underline again, that this is just what Bulgarians are doing. In 2004, the Bulgarian index increased by some 40 per cent, which shows that, like homes, the stock exchange is a primary inflation sector, which benefits from the inrush of new loans. Of course, while the influx of saved money to the stock exchange is characterized as investment, the inrush of new loans to the stock exchange is speculation per se and hence we are justified to define the stock exchange as speculative for the time being.

In fine, this first phase of "low" inflation will not last forever; the day of "high" inflation will come eventually and then – Doomsday, as well. In Section Five we describe Doomsday, as well as what should be done now in order to avoid it and to prevent future financial cataclysms.

Credit and Inflation

The Inflationary Role of Credit

We mentioned loans a couple of times earlier in our analysis. Now we will discuss in more detail this important economic aspect and the role of loans in the inflationary process.

First, we point out that we do not mean only bank loans. There are many loan classifications. Most popular are, perhaps, commercial loans where an enterprise sells products with deferred payment. Other popular loans include consumer and housing loans. For our analysis, it is necessary and sufficient to focus on bank loans, in other words, on loans provided by financial institutions.

The first basic characteristic of the bank loan is that it increases money supply. If Consumer A has a deposit in the bank to the amount of BGN 1000 and the bank, in turn, provides Consumer B with a loan to the amount of BGN 500, then money supply increases from BGN 1000 to BGN 1500 because at the point before the loan total A and B means of payment amount to BGN 1000 and at the point after the loan – to BGN 1500. In other words, bank loans increase money supply and lead to inflation. It is important to note also that to generate inflation, one does not need to print money. It is sufficient for bank loans to grow. It does not mater whether the loan is provided for production, consumption, investment, housing or speculation purposes; ultimately, it is always inflationary.

The second basic characteristic of bank loans is that they raise most the prices in the economic sectors, which they enter first. For example, if most loans in an economy are housing ones, one can expect highest increase of housing prices. If the second largest amount of loans goes to stock exchange, then prices there will swing up as well. Given that in Bulgaria money supply growth is about 20 per cent year on year, then the price increase in all directly credited sectors will be above 20 per cent and in the other sectors – below 20 percent.

Bank loans enable us to understand the first phase of the inflationary process when, for example, money supply growth is 20 per cent, and prices of consumer goods increase by only 5 per cent. The reason is that in the beginning of the inflationary process bank loans are used to purchase assets like production enterprises, mines, homes, shares and bonds, and not for consumer goods like bread and cheese. In this case, prices of assets in the credited sectors increase by more than 20 per cent. For example, in the past 2004, the averaged increase of home prices in Bulgaria is 35 – 40 per cent, of stock exchange prices – 40 per cent, whereas money supply growth is only 20 per cent. Hence, we can conclude that loans finance mainly homes and shares. Of course, they also finance many other sectors like construction and production, but that is a different matter. It is important for us to understand what sectors bank loans enter first.

Credit and Speculation

Bank loans are divided conditionally into productive (investment) loans and speculative loans. Growth in productive loans can approximate economic growth. This is so because productive investments in an economy cannot be higher than gross savings. Hence, investment growth cannot be higher than savings growth in a long-term perspective. Growth in savings, in turn, cannot be much higher than economic growth. Ultimately, growth in investments and investment loans in an economy approximates economic growth. The other loans are speculative. In other words, if economic growth is about 5 per cent and growth in loans is about 50 per cent, growth in production loans is about 5 per cent and the other 45 per cent of the loans incite speculation, which, in Bulgaria, is connected mainly with homes and quoted shares, for the time being.

Thus, we come to the third basic characteristic of fast growing loans – they are speculative in nature. A rough rule of thumb says that short-term growth in production investments cannot be higher than double economic growth. This means that if economic growth is 5 per cent year on year, investments, which can be completed subsequently and not abandoned early, can hardly exceed 10 per cent. Hence, investment loans cannot exceed 10 per cent, and loans above 10 per cent (double economic growth) are called fast growing loans, which are purely speculative in nature. We point out that in this case 10 per cent is a stable and reliable approximation based on many analyses of data accumulated for decades. Those who have read the Christmas issue of Capital Weekly will remember that in the article Chronicle of a Notified Speculation (pp 48-49) we give exactly the same definition of the speculative increase of home prices and clearly demonstrate that the Bulgarian home market is speculative. Now we have clarified the origin of this definition.

Loans and Business Cycles

Finally, we come to the most important characteristic of bank (speculative) loans – business cycle stimulation. This means that when loans increase, they generate economic boom and when loans decrease, they lead to economic crisis. Since loans are inflationary in nature and inflation goes through its phases, it is absolutely impossible to maintain economic boom by permanent loan growth, because with time inflation will change from "low" to "high" and the persistently maintained permanent economic boom will ultimately result in hyperinflation and currency collapse. That is why, some time or another, credit expansion always and ever ends, inevitably leading first to stagnation of the economy and then to recession and, possibly, to severe and ruthless depression. The longer and more sweeping the loan growth has been, the longer and more painful is the recession or depression that follows. Follow-up recession or depression only ends when the banking system is purged of speculative loans. We would love to discuss the business cycle topic in the future, as applied to the situation in Bulgaria.

There are two ways of purging of speculative loans: by repayment and by bankruptcies. Repayment leads to drastic fall in consumption and demand, hence in production and employment, in other words, to painful unemployment. Bankruptcies result in severe losses for the rich and the poor alike. Bankruptcies lead to closing banks and unsatisfied depositors who lose their last savings. Purging of speculative loans ultimately leads to disastrous slump in the prices of speculative assets. Sometimes the price fall is fast and sweeping like in the Great Depression (1929-1932), when home prices decreased ten times and homes lost 90 per cent of their value for 4 years. Sometimes the price fall is slow and lengthy like in Japan of today where stock exchange and home prices have been falling for more than 14 years and in this 14-year period homes have lost about 65 per cent of their value.

Thus, we have substantiated also the need to restrict (administratively) bank loans before it is too late. We will discuss this topic in detail in the last section of this series.

To summarize, bank loans are inflationary and fast growing loans are speculative in nature. Prices in credited sectors increase much faster than total prices in an economy and become speculative. The speculative nature of sectors leads in turn to overinvestment and to bad and unprofitable investments, thus generating economic boom which inevitably ends with a collapse. Under these circumstances, a reasonable State would restrict bank lending.

Restricting Bank Credit

We pointed out in the previous section that bank loans are inflationary and fast growing loans are speculative in nature. Prices in credited sectors increase much faster than total prices in an economy and become speculative. The speculative nature of sectors leads in turn to overinvestment and to bad and unprofitable investments, thus generating economic boom which inevitable ends with a collapse. Under these circumstances, a reasonable government policy would restrict bank lending with a view to minimize the negative effects of speculative loans and of business cycle stimulation.

Deflation

Economic crisis is associated with decreased money supply. During a crisis, active money (banknotes) usually increases slightly while banking system loans squeeze fast. Overall, money supply decreases and leads to deflation, which is opposite to inflation. While inflation leads to price upswing in some economic sectors, deflation leads to fall of these prices. The higher the rise of a price in the inflation period, the more it would fall in the deflation period.

While it is rather easy to forecast the total decline in a sector, housing for example, it is more difficult to predict the pace of such decline. For example, if we estimate the decrease of home prices at 40 per cent, we can have year on year decrease of 40 per cent or 2-year decrease of 20 per cent year on year, or 8-year decrease of 5 per cent year on year.

Deflation and Economic Crises

An economic crisis is characterized by two basic problems: falling prices of speculative assets and bank crises. Two independent forces operate in tandem generating these problems.

The first one is credit crunch. When home and stock exchange prices stabilize and begin to fall, the natural response of banks is to restrict lending. This, in turn, leads to another fall of asset and home prices because loans are the main driver of prices up. However, loans become the main driver of prices down during crisis. Then borrowers have problems paying the loan, which lead to a necessary liquidation of their assets (shares and homes), and that, in turn, results in fall of the prices of such assets.

The second force is of general economic nature. Credit crunch always leads to general economic recession associated with unemployment and decrease of the incomes of businesses and of people. Businesses usually finance their undertakings from their total profit in other sectors and such profit often vanishes during recession. Businesses begin to experience liquidity problems, which, in turn, lead to liquidation of their investments and to fall of the prices of such investments.

A general economic crisis generates employment problems and a reduction of income from salaries and wages. Many members of households with mortgage loans become unemployed and cannot repay their loans. To serve the loans, they have to restrict their consumption in other economic sectors, which aggravates the economic crisis. In an environment of credit contraction and general economic crisis, such people cannot take another loan and many of them have to sell their homes so that banks get back their loans and consumers save at least a portion of their down payment. This generates a wave of housing supply, which further deteriorates the price fall. The effect on the stock exchange is similar, but the wave of selling out speculative investments is much faster and abrupt. This usually results in a stock exchange crash.

In other words, the credit squeeze effect operates in conjunction with the economic crisis one and the two are mutually intensifying. A vicious circle occurs. Falling stock exchange and home prices lead to credit squeeze, or deflation. Deflation, in turn, leads to economic recession, which results in falling stock exchange and home prices and new credit squeeze.

The credit liquidation process ends naturally only when the system is purged of a major portion of the speculative loans. This means that at the end of this process, most of the risk borrowers have lost their homes; the majority of speculators have lost their risk capital and have sold out their shares, and most of the risky banks are in a liquidity crisis or bankruptcy. This is often connected with general liquidity problems across the whole banking system and leads to a general banking crisis. It is important to realize that credit crunch in the banking sector is, in itself, de facto bank crisis. In other words, deflation is of a crisis nature. However, the problem is not in deflation, but in the previous inflation. If it were not for the preceding inflation, there would not be subsequent deflation accompanied by a bank crisis.

It follows from this that the Government and BNB should take drastic measures to restrict bank credit expansion with a view to prevent a future general economic and bank crisis.

Crisis Scenario

What would happen if BNB does not take soon *efficient* measures to restrict lending? In a crisis, the most risky banks will be ruined and so will be their depositors. Government deposit guarantees will not suffice. In such case, assets in a special fund will be needed, but such fund does not exist or will be negligible against the huge deposit losses. Of course, the general government budget would not be able to prevent the crisis, either, because it, in turn, will get finance from nowhere. In an aggravated bank crisis, the budget will pale beside the deposits that will have to be covered. Yet the Government will find a solution: printing the necessary money in order to keep its promise to protect the banks, which will lead to collapse of the Lev.

In other words, in a crisis, something in the system has to give in and someone will have to be ruined. First, it could be the weak banks and, possibly, their depositors. Second, it could be the government budget and the taxpayers. Third, it could be the currency board and all Bulgarians. That is, deflation necessarily leads to losses and it is a matter of government policy and of how the Government will respond to a developing crisis whether these losses will be borne by (1) banks, (2) banks and depositors, (3) taxpayers or the people. The ultimate result cannot be projected on basis of economic analysis, but in this case, we can venture a prognosis based on historical analysis.

History shows, that societies with wild market economy orientation and with the so-called *laissez-faire* economic policy prefer the first two variants while societies with “socialist” orientation prefer the two other. Undoubtedly, the first two variants are preferable from an economic point of view because they make banks and depositors more careful in their decisions, whereas the two other lead to lending race and to a rush to profit from lending because, ultimately, losses will be born by the people and not by the businessmen (bankers). In other words, the first two variants represent market economy afoot and the two other represent reallocation of incomes and making the political and economic upper crust rich at the expense of the people.

Such interpretation makes it clear that in a crisis the Bulgarian State and Government will choose any of the two last variants. This will depend on the level of crisis and on the necessary funds to overcome it. If the budget suffices, it will be the only sacrificed. If it is not sufficient, the Lev will be sacrificed as well. In an environment of a bank crisis and total political pressure, the currency board will have to give in or it will be directly destroyed. The Board independence is a political camouflage, which would be unveiled on the day of crisis. A race to exchange Levs for Euros will begin. Wise people will have long exchanged their money and will realize sizable profit. Those who are late will bear the losses. Winners will be 2-5 per cent of the players. Losers will be 90-95 per cent of the people. This is what history teaches us and we will not miss the opportunity to go through this again, unless bank lending is efficiently restricted in good time in order to prevent bank crisis.

Specific Recommendations to BNB and the Government

Our professional advice to BNB and the Government is to restrict lending growth to 30 per cent in 2005 and 20 per cent in 2006. That would prevent the disastrous scenario described above. The administrative measures, which BNB is implementing, are not efficient enough and banks will keep escaping them. Lending growth restrictions should apply to the whole bank – some other countries have also resorted to this measure. Banks will skillfully escape any other half-measures, which will not have the desired effect. As regards the people, we recommend to all Bulgarians to follow close lending growth and if they are dissatisfied with its restriction, to begin to exchange their Levs for Euros or other stable currencies, but best – for gold and silver.

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2
Economic dynamics														
Industrial production														
Industrial production, volume index, 2000 =100, %														
2005	135.4	138.4	166.0	150.0	142.3	156.6	155.9	149.6					146.6	149.6
2004	122.1	128.3	145.4	130.9	131.8	147.7	145.9	139.2	150.2	149.2	159.6	172.7	131.9	136.8
2003	111.9	107.3	125.5	114.2	108.3	121.4	125.6	117.8	128.3	130.8	130.2	142.1	114.9	114.6
Industrial production, volume index, previous month =100, %														
2005	78.4	102.2	119.9	90.4	94.9	110.0	99.6	96.0					-	-
2004	85.9	105.1	113.3	90.0	100.7	112.1	98.8	95.4	107.9	99.3	107.0	108.2	-	-
2003	93.2	95.9	117.0	91.0	94.8	112.1	103.5	93.8	108.9	101.9	99.5	109.1	-	-
Industrial production, volume index, corresponding period of the previous year = 100, %														
2005	110.9	107.9	114.2	114.6	108.0	106.0	106.9	107.5					111.1	109.4
2004	109.1	119.6	115.9	114.6	121.7	121.7	116.2	118.2	117.1	114.1	122.6	121.5	114.8	119.3
2003	118.9	114.4	122.6	109.8	107.9	113.8	111.9	109.6	114.9	116.6	110.2	118.3	118.7	110.5
Industrial production, from the beginning of the year, volume index, corresponding period of the previous year = 100, %														
2005	110.9	109.3	111.1	112.0	111.2	110.2	109.7	109.4					111.1	110.2
2004	109.1	114.2	114.8	114.8	116.1	117.1	116.9	117.1	117.1	116.8	117.3	117.7	114.8	117.1
2003	118.9	116.7	118.7	116.4	114.7	114.5	114.1	113.5	113.7	114.0	113.6	114.0	118.7	114.5
Industrial sales														
Industrial sales, volume index, 2000 =100, %														
2005	135.8	136.5	171.4	154.4	151.6	166.8	168.9	164.7					147.9	157.6
2004	114.9	126.0	144.8	136.3	132.7	153.4	155.9	143.4	158.6	157.3	167.9	176.1	128.6	140.8
2003	108.1	104.1	124.8	114.1	112.5	122.8	125.9	118.3	125.7	129.7	127.5	138.0	112.3	116.5
Industrial sales, volume index, previous month =100, %														
2005	77.1	100.5	125.6	90.1	98.2	110.0	101.3	97.5					-	-
2004	83.3	109.7	114.9	94.1	97.4	115.6	101.6	92.0	110.6	99.2	106.7	104.9	-	-
2003	91.7	96.3	119.9	91.4	98.6	109.2	102.5	94.0	106.3	103.2	98.3	108.2	-	-
Industrial sales, volume index, corresponding period of the previous year = 100, %														
2005	118.2	108.3	118.4	113.3	114.2	108.7	108.3	114.9					115.0	111.9
2004	106.3	121.0	116.0	119.5	118.0	124.9	123.8	121.2	126.2	121.3	131.7	127.6	114.5	120.9
2003	117.8	115.8	130.0	109.6	116.2	117.1	112.2	110.5	115.2	120.1	113.2	117.0	121.4	114.3

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2
Industrial sales, from the beginning of the year, volume index, corresponding period of the previous year = 100, %														
2005	118.2	113.0	115.0	114.6	114.5	113.4	112.6	112.9					115.0	113.4
2004	106.3	113.5	114.5	115.7	116.2	117.7	118.7	119.0	119.9	120.0	121.1	121.8	114.5	117.7
2003	117.8	116.8	121.4	118.2	117.8	117.6	116.8	115.9	115.8	116.3	116.0	116.1	121.4	117.6
Trade														
Trade and repairing activities, net receipts from sales, volume index, 2000 =100, %														
2005	146.5	145.7	168.6	168.7	166.8	180.5	186.3	196.3					153.6	172.0
2004	126.8	134.4	137.5	136.6	137.1	143.0	153.2	159.2	166.4	168.9	176.3	192.0	132.9	138.9
2003	120.0	127.3	137.3	133.1	135.3	139.1	148.3	149.5	152.5	158.5	149.1	170.0	128.2	135.8
Trade and repairing activities, net receipts from sales, volume index, previous month =100, %														
2005	76.3	99.5	115.7	100.1	98.9	108.2	103.2	105.4					-	-
2004	74.6	106.0	102.3	99.3	100.4	104.3	107.1	103.9	104.5	101.5	104.4	108.9	-	-
2003	82.8	106.1	107.9	96.9	101.7	102.8	106.6	100.8	102.0	103.9	94.1	114.0	-	-
Trade and repairing activities, net receipts from sales, volume index, corresponding period of the previous year = 100, %														
2005	115.5	108.4	122.6	123.5	121.7	126.2	121.6	123.3					115.6	123.8
2004	105.7	105.6	100.1	102.6	101.3	102.8	103.3	106.5	109.1	106.6	118.2	112.9	103.7	102.3
2003	118.0	118.9	119.8	121.3	121.5	119.1	117.8	114.7	116.7	115.8	112.6	117.2	118.9	120.6
Trade and repairing activities, net receipts from sales, volume index, from the beginning of the year, corresponding period of the previous year =100, %														
2005	115.5	111.9	115.6	117.6	118.4	119.8	120.1	120.5					115.6	119.8
2004	105.7	105.6	103.7	103.4	103.0	102.9	103.0	103.5	104.2	104.4	105.8	106.5	103.7	102.9
2003	118.0	118.4	118.9	119.5	119.9	119.8	119.5	118.8	118.5	118.2	117.6	117.6	118.9	119.8
Inflation														
Inflation (Consumer price index - 100), previous month =100, %														
2005	0.7	0.9	0.3	1.1	-0.5	-1.3	0.1	0.6	1.4				-	-
2004	1.4	0.3	-0.1	0.3	0.0	-1.8	1.2	-0.4	0.9	0.2	0.6	1.3	-	-
2003	0.6	0.1	0.4	0.3	-0.6	-2.2	0.9	0.8	0.9	0.7	1.8	1.8	-	-
Inflation (Consumer price index - 100), December of the previous year = 100, %														
2005	0.7	1.6	1.9	3.0	2.6	1.2	1.3	1.9	3.3				-	-
2004	1.4	1.7	1.7	1.9	2.0	0.2	1.4	0.9	1.9	2.0	2.7	4.0	-	-
2003	0.6	0.8	1.2	1.5	0.8	-1.4	-0.5	0.3	1.2	1.9	3.8	5.6	-	-
Inflation (Consumer price index - 100), corresponding period of the previous year = 100, %														
2005	3.3	3.9	4.3	5.1	4.6	5.1	3.9	5.0	5.4				3.8	4.9
2004	6.4	6.6	6.2	6.1	6.8	7.3	7.6	6.3	6.3	5.8	4.5	4.0	6.4	6.7
2003	1.7	0.2	-0.2	0.2	1.7	1.2	2.0	3.5	3.6	3.3	5.1	5.6	0.6	1.1

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2
Employment and unemployment														
Unemployed persons registered, total, end of the period, number														
2005	486 414	485 504	471 296	449 740	427 198	411 586	405 493	399 026					471 296	411 586
2004	537 137	527 258	507 508	487 814	466 717	452 428	446 784	442 190	434 737	437 493	440 039	450 566	507 508	452 428
2003	646 757	611 727	581 350	552 068	528 718	506 424	489 343	480 881	472 614	476 326	489 618	500 664	581 350	506 424
Unemployment (Employment Agency, ratio to the economically active population from the population census in 2001), end of the period, %														
2005	13.13	13.11	12.72	12.14	11.53	11.11	10.95	10.77					12.72	11.11
2004	14.50	14.23	13.7	13.17	12.6	12.21	12.06	11.94	11.74	11.81	11.88	12.16	13.70	12.21
2003	17.46	16.51	15.69	14.90	14.27	13.67	13.21	12.98	12.76	12.86	13.22	13.52	15.69	13.67
Newly opened vacant jobs, for the period, number														
2005	2 466	2 122	4 347	5 298	4 064	4 014	2 959	3 921					-	-
2004	3 286	4 772	5 050	3 538	4 090	4 571	4 085	2 966	3 009	6 232	7 198	2 992	-	-
2003	1 759	2 024	2 136	2 480	2 349	6 076	3 890	2 782	2 804	3 365	3 516	3 999	-	-
Employees, total, end of the period, number														
2005	2 117 190	2 127 571	2 144 669	2 164 483	2 173 806	2 191 194							2 144 669	2 191 194
2004	2 089 842	2 107 924	2 127 689	2 146 489	2 162 177	2 175 873	2 186 757	2 181 207	2 170 404	2 162 474	2 144 427	2 109 478	2 127 689	2 175 873
2003	1 946 834	1 991 623	2 016 828	2 043 764	2 054 972	2 068 694	2 075 881	2 067 291	2 063 429	2 050 282	2 034 033	2 005 369	2 016 828	2 068 694
Employees, public sector, end of the period, number														
2005	702 953	709 595	714 843	713 228	715 097	715 392							714 843	715 392
2004	751 635	759 485	766 657	767 878	769 983	770 520	742 194	738 504	739 786	737 760	733 506	717 920	766 657	770 520
2003	730 873	757 271	765 688	771 192	771 746	775 281	778 647	776 774	778 293	772 629	768 505	758 795	765 688	775 281
Employees, private sector, end of the period, number														
2005	1 414 237	1 417 976	1 429 826	1 451 255	1 458 709	1 475 802							1 429 826	1 475 802
2004	1 338 207	1 348 439	1 361 032	1 378 611	1 392 194	1 405 353	1 444 563	1 442 703	1 430 618	1 424 714	1 410 921	1 391 558	1 361 032	1 405 353
2003	1 215 961	1 234 352	1 251 140	1 272 572	1 283 226	1 293 413	1 297 234	1 290 517	1 285 136	1 277 653	1 265 528	1 246 574	1 251 140	1 293 413
Employees, total, end of the period, growth to corresponding month of previous year=100														
2005	1.3	0.9	0.8	0.8	0.5	0.7							0.8	0.7
2004	7.3	5.8	5.5	5.0	5.2	5.2	5.3	5.5	5.2	5.5	5.4	5.2	5.5	5.2
2003	3.6	5.7	6.7	7.8	7.8	8.1	8.2	8.0	7.2	6.9	6.0	4.9	6.7	8.1
Employees, public sector, end of the period, growth to corresponding month of previous year=100														
2005	-6.5	-6.6	-6.8	-7.1	-7.1	-7.2							-6.8	-7.2
2004	2.8	0.3	0.1	-0.4	-0.2	-0.6	-4.7	-4.9	-4.9	-4.5	-4.6	-5.4	0.1	-0.6
2003	-4.0	-0.6	0.7	2.8	3.5	4.3	5.6	5.6	5.1	5.0	2.8	0.3	0.7	4.3

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2
Employees, private sector, end of the period, growth to corresponding month of previous year=100														
2005	5.7	5.2	5.1	5.3	4.8	5.0							5.1	5.0
2004	10.1	9.2	8.8	8.3	8.5	8.7	11.4	11.8	11.3	11.5	11.5	11.6	8.8	8.7
2003	8.9	10.1	10.8	11.0	10.6	10.5	9.9	9.5	8.5	8.1	8.1	8.0	10.8	10.5
Fiscal review														
State budget														
Revenues of the Consolidated State Budget, total, BGN million														
2005	1 326.2	2 536.1	4 166.5	5 759.6	7 349.7	8 846.2	10 302.7	11 758.7					4 166.5	8 846.2
2004	1 126.0	2 110.6	3 636.8	5 097.6	6 375.6	7 646.9	8 996.5	10 311.4	11 622.1	12 978.2	14 304.5	15 858.1	3 636.8	7 646.9
2003	1 029.2	1 944.8	3 220.6	4 631.2	5 813.3	6 830.5	8 054.1	9 158.9	10 311.4	11 573.2	12 657.0	14 072.0	3 220.6	6 830.5
Expenditures of the Consolidated State Budget, total, BGN million														
2005	1 238.2	2 401.7	3 687.1	5 086.4	6 354.9	7 719.0	9 169.4	10 440.4					3 687.1	7 719.0
2004	1 152.7	2 260.2	3 408.4	4 568.7	5 665.8	6 769.3	8 019.8	9 119.7	10 322.3	11 502.8	12 826.5	15 198.9	3 408.4	6 769.3
2003	1 130.6	2 105.4	3 109.8	4 221.5	5 195.0	6 203.4	7 402.7	8 429.7	9 463.7	10 602.5	11 758.1	14 071.1	3 109.8	6 203.4
Consolidated State Budget deficit (-) /surplus (+), BGN million														
2005	88.0	134.4	479.3	673.1	994.8	1 127.3	1 133.3	1 318.2					479.3	1 127.3
2004	-26.7	-149.5	228.4	528.9	709.7	877.6	976.7	1191.7	1299.7	1475.3	1478.0	659.2	228.4	877.6
2003	-101.5	-160.6	110.8	409.7	618.3	627.1	651.4	729.2	847.8	970.7	898.9	0.9	110.8	627.1
Revenues of the Republican Budget, total, BGN million														
2005	908.8	1 670.6	2 756.1	3 865.8	4 935.5	5 890.1	6 840.9	7 779.6					2 756.1	5 890.1
2004	777.1	1 368.7	2 343.4	3 368.2	4 241.3	5 098.0	5 912.6	6 764.3	7 571.6	8 434.5	9 276.0	10 186.8	2 343.4	5 098.0
2003	651.3	908.4	1 937.0	2 878.1	3 626.4	4 221.2	4 985.2	5 637.7	6 279.0	7 051.8	7 684.9	8 441.6	1 937.0	4 221.2
Expenditures of the Republican Budget, total, BGN million														
2005	859.6	1624.7	2355.2	3242.2	4008.8	4 882.4	5 839.4	6 580.7					2 355.2	4 882.4
2004	841.2	1 531.5	2 222.5	2 963.0	3 640.1	4 315.5	5 134.6	5 773.9	6 575.3	7 249.0	8 019.3	9 757.0	2 222.5	4 315.5
2003	737.0	1 195.6	1 846.2	2 594.1	3 016.6	3 639.2	4 372.7	4 979.0	5 520.4	6 200.7	6 952.7	8 552.2	1 846.2	3 639.2
Republican Budget cash deficit (-) / surplus (+), BGN million														
2005	49.2	45.9	400.9	623.6	926.7	1 007.7	1 001.5	1 198.9					400.9	1 007.7
2004	-64.0	-162.8	120.9	405.3	601.2	782.4	778.0	990.4	996.3	1 185.6	1 256.6	429.7	120.9	782.4
2003	-85.7	-287.2	90.8	284.0	609.7	582.0	612.4	658.7	758.5	851.1	732.2	110.6	90.8	582.0

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2
Government and government guaranteed debt														
Government and government guaranteed debt, BGN million														
2005	14 387.5	14 210.7	14 319.2	14 382.2	14 635.9	14 689.7	13 755.2	13 519.7					14 319.2	14 689.7
2004	16 731.7	16 852.8	17 032.7	17 332.8	17 187.1	17 198.8	16 089.2	16 068.7	16 054.2	15 927.5	15 677.9	15 557.3	17 032.7	17 198.8
2003	17 547.9	17 638.7	17 560.2	17 679.7	17 062.1	17 364.8	17 466.7	17 858.3	17 194.7	17 140.1	16 930.8	16 509.7	17 560.2	17 364.8
Domestic government and government guaranteed debt, BGN million														
2005	2 700.2	2 724.9	2 732.1	2 732.5	2 768.1	2 772.2	2 847.1	2 794.7					2 732.1	2 772.2
2004	2 331.3	2 397.3	2 425.6	2 462.3	2 475.3	2 494.5	2 494.7	2 536.8	2 568.9	2 597.8	2 627.4	2 680.6	2 425.6	2 494.5
2003	2 113.5	2 207.4	2 290.7	2 246.2	2 225.5	2 233.9	2 215.4	2 236.5	2 218.1	2 193.7	2 248.4	2 241.2	2 290.7	2 233.9
Foreign government and government guaranteed debt, BGN million														
2005	11 687.3	11 485.8	11 587.1	11 649.9	11 867.8	11 917.5	10 908.1	10 725.0					11 587.1	11 917.5
2004	14 400.4	14 455.5	14 607.1	14 870.4	14 711.9	14 704.3	13 594.6	13 531.8	13 485.4	13 329.8	13 050.7	12 876.6	14 607.1	14 704.3
2003	15 434.4	15 431.3	15 269.8	15 433.7	14 836.3	15 131.1	15 251.2	15 621.8	14 976.6	14 946.6	14 683.4	14 268.6	15 269.8	15 131.1
Government and government guaranteed debt, ratio to the annual GDP, %														
2005	34.8	34.4	34.6	34.8	35.4	35.5	33.3	32.7					34.6	35.5
2004	44.1	44.4	44.8	45.6	45.2	45.3	42.4	42.3	42.3	41.9	41.3	40.9	44.8	45.3
2003	49.7	50.0	49.8	50.1	48.4	49.2	49.5	50.6	48.7	48.6	48.0	47.8	49.8	49.2
Domestic government and government guaranteed debt, ratio to the annual GDP, %														
2005	6.5	6.6	6.6	6.6	6.7	6.7	6.9	6.8					6.6	6.7
2004	6.1	6.3	6.4	6.5	6.5	6.6	6.6	6.7	6.8	6.8	6.9	7.0	6.4	6.6
2003	6.0	6.3	6.5	6.4	6.3	6.3	6.3	6.3	6.3	6.2	6.4	6.5	6.5	6.3
Foreign government and government guaranteed debt, ratio to the annual GDP, %														
2005	28.3	27.8	28.0	28.2	28.7	28.8	26.4	25.9					28.0	28.8
2004	37.9	38.1	38.5	39.2	38.7	38.7	35.8	35.6	35.5	35.1	34.4	33.8	38.5	38.7
2003	43.7	43.7	43.3	43.7	42.0	42.9	43.2	44.3	42.4	42.4	41.6	41.3	43.3	42.9
Domestic government debt, total, BGN million														
2005	2 700.2	2 724.9	2 732.1	2 732.4	2 768.0	2 772.3	2 847.1	2 794.7					2 732.1	2 772.3
2004	2 331.3	2 397.2	2 425.7	2 462.3	2 475.3	2 494.5	2 494.7	2 536.8	2 568.9	2 597.8	2 627.4	2 680.6	2 425.7	2 494.5
2003	2 111.6	2 205.8	2 289.4	2 245.3	2 225.1	2 233.9	2 215.5	2 236.5	2 218.2	2 193.6	2 248.4	2 241.1	2 289.4	2 233.9
Debt on Government Securities issued for budget deficit financing, BGN million														
2005	2 253.3	2 281.4	2 284.3	2 284.5	2 309.5	2 309.6	2 384.6	2 334.1					2 284.3	2 309.6
2004	1 822.7	1 889.3	1 914.9	1 949.0	1 967.8	1 986.8	1 985.9	2 033.6	2 072.6	2 112.2	2 151.6	2 211.2	1 914.9	1 986.8
2003	1 515.4	1 608.5	1 696.0	1 658.9	1 658.5	1 658.2	1 637.7	1 652.5	1 653.9	1 633.2	1 696.7	1 703.9	1 696.0	1 658.2

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2
Debt on Government Securities issued for structural reform, BGN million														
2005	447.0	443.5	447.7	447.9	458.5	462.7	462.5	460.6					447.7	462.7
2004	508.6	508.0	510.8	513.3	507.4	507.6	508.9	503.2	496.3	485.6	475.8	469.5	510.8	507.6
2003	596.2	597.2	593.4	586.4	566.6	575.7	577.7	584.0	564.3	560.4	551.6	537.2	593.4	575.7
Foreign government debt, USD million														
2005	7 198.4	7 189.7	7 090.0	7 094.8	6 872.8	6 771.9	6 146.5	6 083.5					7 090.0	6 771.9
2004	8 620.0	8 635.2	8 587.7	8 545.4	8 621.3	8 587.6	7 815.4	7 821.0	8 004.8	8 117.7	8 286.0	8 362.7	8 587.7	8 587.6
2003	8 109.3	8 091.6	8 090.0	8 355.8	8 535.8	8 414.6	8 372.2	8 284.1	8 461.0	8 417.2	8 530.4	8 718.6	8 090.0	8 414.6
Foreign government guaranteed debt, USD million														
2005	590.7	595.6	590.4	623.7	593.5	596.1	597.9	605.4					590.4	596.1
2004	498.1	542.9	541.8	538.0	554.2	550.7	552.7	558.2	551.1	563.0	585.4	604.8	541.8	550.7
2003	426.3	415.3	416.0	427.8	432.0	425.8	453.4	443.6	461.3	464.3	473.5	495.5	416.0	425.8
Foreign economic relations and foreign investments														
Balance of Payments														
Current account, million USD														
2005	-366.8	-240.1	-306.5	-365.7	-352.2	-214.3	-103.6	-142.0					-913.4	-932.2
2004	-309.3	-178.4	-187.1	-285.9	-278.3	-47.4	243.2	157.1	29.1	-276.0	-485.2	-435.2	-674.8	-611.6
2003	-183.1	-162.8	-100.6	-408.0	-256.0	20.6	22.3	136.1	-1.3	-250.5	-327.7	-344.9	-446.5	-643.4
Trade balance, (FOB), million USD														
2005	-260.5	-273.3	-320.5	-361.4	-498.2	-448.7	-377.6	-484.6					-854.3	-1 308.3
2004	-195.1	-184.5	-256.1	-322.5	-370.3	-264.3	-164.6	-213.4	-193.2	-296.6	-465.6	-440.2	-635.7	-957.1
2003	-72.3	-121.4	-118.3	-273.2	-302.0	-161.1	-205.5	-155.1	-149.4	-262.2	-321.1	-376.9	-312.0	-736.3
Exports (FOB), million USD														
2005	838.4	841.1	1045.2	966.0	934.5	997.6	1033.6	958.2					2 724.7	2 898.1
2004	631.5	735.6	779.6	716.0	720.4	847.0	963.6	812.2	893.5	922.7	950.6	875.0	2 146.7	2 283.4
2003	564.8	542.0	648.5	585.5	596.0	657.2	708.1	604.5	657.7	704.6	635.0	636.9	1 755.3	1 838.7
Imports (FOB), million USD														
2005	-1098.8	-1114.5	-1365.7	-1327.5	-1432.7	-1446.3	-1411.2	-1442.8					-3 579.0	-4 206.5
2004	-826.6	-920.1	-1035.7	-1038.5	-1090.7	-1111.3	-1128.2	-1025.6	-1086.6	-1219.3	-1416.1	-1315.2	-2 782.4	-3 240.5
2003	-637.1	-663.4	-766.7	-858.7	-898.0	-818.3	-913.6	-759.6	-807.1	-966.8	-956.0	-1 013.8	-2 067.2	-2 575.0
Services, net, million USD														
2005	-35.0	-29.3	-34.6	-68.9	54.9	207.8	307.7	297.5					-98.9	193.8
2004	-25.5	0.9	-10.8	-53.4	80.3	220.1	342.7	315.2	142.6	-29.0	-59.4	-46.7	-35.4	247.0
2003	-22.4	-14.9	-24.5	-35.9	30.9	169.1	238.1	238.6	124.4	-23.2	-45.6	-41.2	-61.8	164.1

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	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2
Income, net, million USD														
2005	-129.8	-17.0	-39.6	-18.5	-18.6	-81.0	-126.2	-41.9					-186.4	-118.1
2004	-147.2	-48.5	-24.3	-8.6	-54.2	-55.6	-83.0	-47.4	-37.8	-52.9	-58.2	-40.1	-220.0	-118.4
2003	-128.9	-54.7	-25.5	-144.8	-29.5	-45.7	-75.2	-20.4	-55.4	-14.2	-13.9	-18.3	-209.1	-220.0
Current transfers, net, million USD														
2005	58.5	79.6	88.2	83.1	109.8	107.7	92.5	87.0					226.3	300.6
2004	58.6	53.8	104.2	98.5	65.8	52.3	148.1	102.8	117.5	102.6	98.0	91.9	216.6	216.6
2003	40.5	28.2	67.7	45.9	44.7	58.3	64.9	73.0	79.0	49.1	52.8	91.5	136.4	148.9
Capital account, million USD														
2005	0.0	0.1	0.0	-1.2	0.0	0.0	0.0	0.0					0.1	-1.2
2004	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
2003	0.0	0.0	0.0	0.0	0.0	0.0	0.0	-0.1	-0.1	-0.1	0.0	0.0	0.0	0.0
Financial account, million USD														
2005	-172.6	782.2	758.8	324.6	554.7	245.9	-453.3	205.9					1 368.4	1 125.2
2004	-80.4	393.1	262.6	153.4	503.8	586.8	-909.1	220.0	264.9	389.3	593.9	694.6	575.3	1 244.0
2003	33.8	111.5	199.5	536.1	263.2	184.9	30.1	130.5	138.2	560.5	261.5	191.0	344.8	984.2
Direct investment net, million USD														
2005	139.4	41.7	280.5	180.1	168.8	40.3	542.7	133.7					461.6	389.2
2004	171.1	145.8	158.6	59.3	138.6	658.7	-840.3	88.6	48.7	258.2	420.1	918.4	475.5	856.6
2003	134.6	119.2	194.9	153.9	226.4	159.1	214.9	141.6	130.5	397.2	64.3	133.6	448.7	539.4
Direct investment abroad, million USD														
2005	-8.6	-7.4	-4.7	-3.8	-2.5	-0.1	-10.4	-3.8					-20.7	-6.4
2004	-7.2	-2.7	-5.6	-1.2	-1.5	-2.8	-3.1	-0.2	-2.9	-6.5	254.5	-0.4	-15.5	-5.5
2003	-5.8	-0.3	-1.5	-1.5	0.6	-0.5	0.4	-4.3	-2.5	-1.5	-1.3	-8.4	-7.6	-1.4
Direct investment in Bulgaria, million USD														
2005	148.0	49.1	285.2	183.8	171.3	93.0	180.9	137.5					482.3	448.1
2004	178.3	148.5	164.2	60.5	140.1	443.0	180.2	88.8	51.6	264.7	165.6	918.8	491.0	643.6
2003	140.4	119.6	196.3	155.3	225.8	159.6	214.5	145.9	133.0	398.8	65.7	142.0	456.3	540.7
Mergers and acquisitions net, million USD														
2005	0.0	0.0	0.0	0.0	0.0	-52.7	372.1	0.0					0.0	-52.7
2004	0.0	0.0	0.0	0.0	0.0	218.5	-1017.3	0.0	0.0	0.0	0.0	0.0	0.0	218.5
2003	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

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	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2
Portfolio investment assets, million USD														
2005	249.7	-172.8	-112.5	136.2	48.5	-32.8	15.0	-45.2					-35.6	151.9
2004	-64.5	-17.3	36.6	-71.9	27.6	28.2	43.9	18.2	35.4	25.7	249.0	-298.9	-45.2	-16.1
2003	13.5	9.9	-19.8	10.8	87.3	-37.2	-87.3	-55.9	29.3	-36.7	24.9	-18.6	3.6	60.9
Portfolio investment liabilities, million USD														
2005	-965.0	45.3	0.7	18.5	93.9	76.5	-459.1	11.1					-919.0	188.9
2004	-106.3	-48.9	43.1	-15.7	8.1	125.0	-747.8	-11.5	25.6	-4.2	28.2	18.8	-112.1	117.4
2003	-34.5	-13.4	-22.9	0.4	27.9	1.4	-79.4	-16.7	9.0	-14.9	5.5	4.5	-70.8	29.7
Other investment assets, million USD														
2005	516.1	280.3	-132.7	59.7	-3.1	-131.0	-17.8	-39.6					663.7	-74.4
2004	-184.9	72.4	-123.3	106.7	95.8	-418.3	18.4	5.0	-63.1	-71.9	72.4	-432.3	-235.8	-215.8
2003	-10.3	20.1	-55.2	285.6	-123.4	-37.0	-46.1	100.6	-139.6	174.5	114.0	-32.3	-45.4	125.2
Other investment liabilities, million USD														
2005	-112.8	587.7	722.7	-69.8	246.6	292.9	-534.1	145.9					1 197.6	469.7
2004	104.2	241.2	147.6	74.9	233.7	193.2	616.7	119.6	218.4	181.5	-175.8	488.7	493.0	501.8
2003	-69.5	-24.4	102.6	85.4	45.0	98.6	28.1	-39.1	109.0	40.3	52.8	103.9	8.7	229.0
Net Errors and Omissions (BP), million USD														
2005	-106.0	-340.7	-158.1	250.7	188.2	253.8	-33.7	165.0					-604.8	692.7
2004	7.5	-71.9	127.4	207.1	134.9	-41.1	90.1	-6.0	-48.4	167.8	207.4	-81.0	63.0	300.9
2003	-150.5	96.4	-16.6	46.9	97.5	-137.7	-54.1	-149.4	-62.1	21.1	174.6	78.5	-70.7	6.7
Overall balance (BP), million USD														
2005	-645.5	201.5	294.2	208.4	390.7	285.4	-590.6	228.9					-149.8	884.5
2004	-382.1	142.8	202.9	74.6	360.4	498.3	-575.8	371.1	245.6	281.1	316.0	178.4	-36.4	933.3
2003	-299.8	45.1	82.3	175.0	104.7	67.8	-1.6	117.1	74.7	331.1	108.4	-75.4	-172.4	347.5
Reserves and Related Items, million USD														
2005	645.5	-201.5	-294.2	-208.4	-390.7	-285.4	590.6	-228.9					149.8	-884.5
2004	382.1	-142.8	-202.9	-74.6	-360.4	-498.3	575.8	-371.1	-245.6	-281.1	-316.0	-178.4	36.4	-933.3
2003	299.8	-45.1	-82.3	-175.0	-104.7	-67.8	1.6	-117.1	-74.7	-331.1	-108.4	75.4	172.4	-347.5
Finance														
Financial indicators														
Exchange rate BGN / USD, average for the period														
2005	1.49095	1.50304	1.48228	1.51176	1.54322	1.60785	1.62492	1.59115	1.59728				1.49209	1.55428
2004	1.54992	1.54671	1.59447	1.63352	1.63153	1.61138	1.59469	1.60646	1.60010	1.5663	1.50571	1.46055	1.56370	1.62548
2003	1.84170	1.81554	1.81026	1.80353	1.68361	1.67717	1.72003	1.75641	1.74550	1.67286	1.67178	1.59306	1.82250	1.72144

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2
Exchange rate BGN / USD, end of the period														
2005	1.50044	1.47532	1.50866	1.50948	1.58611	1.61746	1.61732	1.6034	1.62417				1.50866	1.61746
2004	1.57932	1.57500	1.59999	1.63709	1.60340	1.60907	1.62428	1.61492	1.57614	1.53555	1.47110	1.43589	1.59999	1.60907
2003	1.80827	1.81393	1.79516	1.75710	1.65440	1.71159	1.72807	1.78991	1.67854	1.68287	1.63067	1.54856	1.79516	1.71159
Basic interest rate, effective annual, average for the period														
2005	2.41	1.91	1.93	1.97	2.05	2.08	2.06	2.06					2.08	2.03
2004	2.82	2.52	2.44	2.58	2.86	3.84	2.46	2.45	2.42	2.42	2.44	2.38	2.59	3.09
2003	3.27	2.53	2.55	2.60	2.98	2.92	2.54	2.55	2.59	2.62	2.63	2.69	2.78	2.83
Money (M1), BGN million														
2005	10 045	10 201	11 331	10 552	10 790	11 167	11 494	11 713					11 331	11 167
2004	7 788	7 853	7 835	7 987	8 036	8 422	8 736	9 048	9 239	9 220	9 185	10 298	7 835	8 422
2003	6 291	6 377	6 274	6 435	6 560	6 834	7 110	7 314	7 416	7 422	7 377	8 030	6 274	6 834
Money (M2), BGN million														
2005	20 438	20 705	23 176	21 990	22 426	22 749	23 200	23 650					23 176	22 749
2004	16 439	16 655	16 678	17 081	17 270	18 033	18 293	18 282	18 675	18 777	18 791	20 302	16 678	18 033
2003	13 551	13 723	13 542	13 762	13 766	14 197	14 624	15 046	15 073	15 698	15 605	16 465	13 542	14 197
International reserves of BNB, BGN million														
2005	12 328	12 785	13 198	13 507	14 075	14 577	13 582	13 912					13 198	14 577
2004	9 841	10 112	10 494	10 605	11 167	11 953	11 033	11 607	12 163	12 576	12 996	13 242	10 494	11 953
2003	8 363	8 473	8 603	9 233	9 316	9 451	9 518	9 800	9 882	10 413	10 557	10 383	8 603	9 451
Fiscal reserves at the Issue Department of BNB, BGN million														
2005	3 370	3 756	4 265	4 475	4 781	4 804	4 130	4 101					4 265	4 804
2004	3 138	3 147	3 503	3 823	4 204	4 803	3 663	4 347	4 642	4 898	5 384	4 346	3 503	4 803
2003	2 793	2 804	3 028	3 633	3 873	3 747	3 766	3 767	3 832	3 971	4 177	3 280	3 028	3 747
Banking system														
Claims on credits granted by the Commercial Banks, total, BGN thousand														
2005	14 339 642	14 669 727	18 216 389	16 403 694	16 444 686	16 239 981	16 506 380	16 805 164					18 216 389	16 239 981
2004	9565122 [1)]	9 848 840	10 247 405	10 659 517	11 008 716	11 309 097	11 877 533	12 076 182	12 526 708	12 954 946	13 410 638	13 939 177	10 247 405	11 309 097
2003	6 444 818	6 563 130	6 816 766	7 167 024	7 424 452	7 727 590	7 866 307	8 171 994	8 471 157	8 904 325	9 114 301	9 454 164	6 816 766	7 727 590
Credits to Resident Sector, total														
2005	14 171 157	14 493 674	17 780 891	16 150 886	16 214 983	16 021 571	16 248 739	16 546 262					17 780 891	16 021 571
2004	9 465 473	9 747 743	10 131 312	10 545 411	10 904 864	11 189 803	11 754 355	11 938 957	12 379 729	12 803 003	13 253 413	13 782 870	10 131 312	11 189 803
2003	6 356 088	6 489 721	6 745 467	7 094 504	7 355 881	7 657 439	7 797 284	8 092 008	8 391 057	8 832 873	9 044 229	9 352 878	6 745 467	7 657 439

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2
Credits to Government Sector														
2005	26 797	26 657	25 976	26 123	26 748	27 319	28 387	30 592					25 976	27 319
2004	24 891	27 795	26 973	26 451	26 628	28 026	28 586	28 556	28 361	28 265	28 505	26 760	26 973	28 026
2003	8 673	8 947	9 494	9 380	9 406	9 561	11 924	13 394	19 928	21 667	22 168	24 635	9 494	9 561
Credits to Non-government Sector														
2005	14 132 460	14 455 119	17 736 034	16 100 296	16 163 770	15 969 789	16 200 835	16 496 153					17 736 034	15 969 789
2004	9 440 582	9 719 596	10 104 001	10 518 659	10 877 937	11 161 514	11 720 617	11 905 251	12 346 446	12 769 818	13 219 990	13 744 209	10 104 001	11 161 514
2003	6 291 902	6 444 260	6 662 763	7 014 528	7 280 799	7 603 463	7 727 111	8 030 421	8 325 688	8 751 119	8 977 126	9 303 120	6 662 763	7 603 463
Credits to Non-financial Public Corporations														
2005	253 924	242 027	263 587	244 253	240 597	225 757	225 986	232 000					263 587	225 757
2004	-	245 972	231 880	232 625	244 408	243 272	226 689	207 946	225 757	266 988	261 609	261 341	231 880	243 272
2003	219 215	229 954	235 631	246 234	245 746	231 489	245 251	237 021	230 292	213 420	217 489	234 230	235 631	231 489
Credits to Non-financial Private Corporations														
2005	9 112 979	9 287 240	11 809 556	10 227 007	10 100 241	9 902 236	9 922 963	10 022 347					11 809 556	9 902 236
2004	6785654 [2)]	6 685 783	6 932 080	7 194 675	7 378 415	7 452 693	7 840 566	7 883 985	8 140 365	8 346 028	8 512 148	8 812 722	6 932 080	7 452 693
2003	4 715 900	4 800 569	4 949 708	5 202 209	5 377 904	5 604 204	5 575 897	5 774 664	5 956 901	6 287 344	6 412 770	6 641 717	4 949 708	5 604 204
Credits to Households and NPISH														
2005	4 458 783	4 610 873	5 095 569	5 335 284	5 525 828	5 686 183	5 887 706	6 057 137					5 095 569	5 686 183
2004	2 530 436	2 655 236	2 802 335	2 950 438	3 107 317	3 302 537	3 487 977	3 644 450	3 806 347	3 976 297	4 158 518	4 373 864	2 802 335	3 302 537
2003	1 260 492	1 300 531	1 355 108	1 438 127	1 532 501	1 645 779	1 758 072	1 853 587	1 933 809	2 035 462	2 116 719	2 201 298	1 355 108	1 645 779
Credits to Non-bank Financial Institutions														
2005	306 774	314 979	567 322	293 752	297 104	155 613	164 180	184 669					567 322	155 613
2004	124 492	132 605	137 706	140 921	147 797	163 012	165 385	168 870	173 977	180 505	287 715	296 282	137 706	163 012
2003	96 295	113 206	122 316	127 958	124 648	121 991	147 891	165 149	204 686	214 893	230 148	225 875	122 316	121 991
Credits to Monetary Financial Institutions														
2005	11 900	11 898	18 881	24 467	24 465	24 463	19 517	19 517					18 881	24 463
2004	-	352	338	301	299	263	5 152	5 150	4 922	4 920	4 918	11 901	338	263
2003	55 513	36 514	73 210	70 596	65 676	44 415	58 249	48 193	45 441	60 087	44 935	25 123	73 210	44 415
Credits to Non-resident Sector														
2005	168 485	176 053	435 498	252 808	229 703	218 410	257 641	258 902					435 498	218 410
2004	99 649	101 097	116 093	114 106	103 852	119 294	123 178	137 225	146 979	151 943	157 225	156 307	116 093	119 294
2003	88 730	73 409	71 299	72 520	68 571	70 151	69 023	79 986	80 100	71 452	70 072	101 286	71 299	70 151

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2
Total assets, end of the period, BGN thousand														
2005	24 597 489	25 134 799	29 073 279	27 506 218	27 578 273	27 926 520	28 118 573	28 827 257					29 073 279	27 926 520
2004	17 530 661	18 005 393	18 756 066	19 144 405	19 229 222	20 096 015	20 651 822	20 959 108	21 549 780	22 300 151	22 650 627	24 917 359	18 756 066	20 096 015
2003	14 470 798	14 527 980	14 976 602	14 754 441	14 752 332	15 359 751	15 706 435	16 019 647	16 386 230	16 621 238	16 608 301	17 323 643	14 976 602	15 359 751
Total liabilities , end of the period, BGN thousand														
2005	21 775 872	22 285 847	26 152 791	24 533 344	24 627 576	24 893 565	25 026 632	25 610 389					26 152 791	24 893 565
2004	15 198 323	15 634 800	16 340 560	16 727 099	16 843 176	17 660 577	18 158 670	18 410 401	18 959 571	19 673 263	19 947 650	22 185 115	16 340 560	17 660 577
2003	12 413 277	12 474 347	12 882 639	12 702 089	12 694 628	13 252 494	13 584 220	13 870 342	14 218 293	14 410 754	14 364 457	15 042 658	12 882 639	13 252 494
Interest revenues, BGN thousand														
2005	138 909	274 979	429 683	585 459	744 411	906 462	1 071 346	1 238 346					429 683	906 462
2004	96 863	194 892	299 962	406 956	519 732	637 944	755 537	877 578	1 000 921	1 128 028	1 258 998	1 391 229	299 962	637 944
2003	74 730	145 393	223 314	302 382	385 403	465 864	550 315	636 814	724 416	816 202	908 081	1 012 487	223 314	465 864
Current profit/loss, BGN thousand														
2005	61 908	85 653	128 889	181 898	200 851	277 482	337 959	403 667					128 889	277 482
2004	41 497	78 677	114 157	132 792	169 150	224 081	257 720	300 494	335 347	366 104	420 992	434 112	114 157	224 081
2003	98 482	122 770	125 420	148 232	180 278	218 487	242 268	266 588	293 663	322 514	355 375	379 817	125 420	218 487
Social policy and industrial relations														
Wage&Salary [3)]														
Average Monthly Wage&Salary of employees under labor contract, total, nominal, BGN														
2005	303	302	319	313	322	317							308	317
2004	277	277	290	287	295	289	295	291	303	296	303	320	281	290
2003	264	259	274	272	280	274	276	273	286	276	286	302	266	275
Average Monthly Wage&Salary of employees under labor contract, public sector, nominal, BGN														
2005	360	363	386	380	408	394							370	394
2004	327	321	350	335	361	343	351	349	375	354	366	400	333	346
2003	308	299	325	318	340	327	326	324	352	326	344	368	311	328
Average Monthly Wage&Salary of employees under labor contract, private sector, nominal, BGN														
2005	275	272	285	280	279	279							277	279
2004	249	251	256	260	257	258	265	261	265	265	269	278	252	258
2003	238	234	242	244	242	241	244	242	245	245	249	260	238	242
Real Average Monthly Wage&Salary of employees under labor contract, total, growth, corresponding period of the previous year =100, %														
2005	5.9	5.0	5.5	3.8	4.4	4.4							5.4	4.2
2004	-1.4	0.3	-0.3	-0.6	-1.4	-1.7	-0.7	0.2	-0.4	1.4	1.4	1.9	-0.5	-1.2
2003	5.9	5.0	6.8	7.2	5.8	5.3	4.4	2.2	4.1	1.5	3.5	4.7	5.9	6.1

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2
Real Average Monthly Wage&Salary of employees under labor contract, public sector, growth, corresponding period of the previous year =100, %														
2005	6.5	8.9	5.8	7.9	8.1	9.3							7.0	8.4
2004	-0.2	0.7	1.4	-0.7	-0.6	-2.2	0.0	1.3	0.2	2.7	1.8	4.5	0.6	-1.2
2003	7.3	4.7	7.1	6.4	5.1	3.8	3.4	0.3	3.5	-1.7	2.6	4.9	6.4	5.1
Real Average Monthly Wage&Salary of employees under labor contract, private sector, growth, corresponding period of the previous year =100, %														
2005	6.9	4.3	6.8	2.5	3.8	2.9							6.0	3.1
2004	-1.7	0.6	-0.3	0.4	-0.6	-0.2	0.9	1.4	1.7	2.3	3.4	2.8	-0.5	-0.1
2003	6.8	6.6	7.7	9.1	6.7	7.2	4.9	3.9	4.1	3.5	3.5	4.3	7.0	7.7
Income and consumption of the households [3]														
Total income, monthly, average per person, nominal, BGN														
2005	156.7	147.6	162.9	175.6	178.8	177.3	183.2	190.9					155.7	177.3
2004	141.3	135.6	148.7	157.4	161.7	161.9	183.8	172.5	176.8	171.6	176.4	219.1	141.8	160.3
2003	128.8	122.4	135.8	142.4	146.6	152.3	157.2	157.0	157.0	156.2	162.1	210.6	129.0	147.1
Cash income, monthly, average per person, nominal, BGN														
2005	152.2	144.5	158.1	167.4	167.5	166.3	170.1	176.6					151.6	167.1
2004	136.4	131.9	143.0	145.0	147.3	150.5	154.5	156.6	160.8	158.3	157.2	189.9	137.1	147.6
2003	124.5	118.3	130.2	132.5	134.2	139.1	142.2	142.0	142.2	140.7	137.2	175.3	124.3	135.3
Total expenditure, monthly, average per person, nominal, BGN														
2005	144.4	138.7	157.0	165.7	170.0	171.9	175.4	182.8					146.7	169.2
2004	140.5	131.6	142.0	156.4	160.0	151.6	176.2	169.5	177.7	169.0	170.2	204.0	138.1	156.0
2003	125.2	116.0	130.1	135.4	143.2	141.8	147.1	151.1	153.1	154.9	153.3	197.9	123.8	140.2
Cash expenditure, monthly, average per person, nominal, BGN														
2005	140.3	135.9	152.5	157.8	159.2	161.1	163.0	168.9					142.9	159.4
2004	136.3	128.3	136.9	146.8	148.0	140.7	163.2	155.7	164.3	156.2	153.3	175.7	133.9	145.1
2003	121.1	112.3	124.9	126.0	131.4	129.7	133.2	137.0	139.3	140.4	134.9	163.6	119.4	129.0
Real total income, monthly, average per person, growth, corresponding period of the previous year =100, %														
2005	7.4	4.8	5.1	6.2	5.8	4.3	-4.1	5.4					5.8	5.4
2004	3.1	3.9	3.1	4.2	3.3	-0.9	8.6	3.4	5.9	3.8	4.1	0.1	3.3	2.1
2003	11.6	7.9	7.5	8.7	5.5	11.1	12.2	6.3	2.0	3.0	7.0	2.0	8.9	8.5
Real cash income, monthly, average per person, growth, corresponding period of the previous year =100, %														
2005	8.0	5.4	6.0	9.8	8.7	5.2	6.0	7.4					6.5	7.9
2004	3.0	4.6	3.5	3.1	2.7	0.9	0.9	3.7	6.4	6.4	9.6	4.2	3.7	2.2
2003	11.9	7.7	7.8	8.3	7.1	11.2	11.7	6.6	1.3	2.9	3.4	5.7	9.1	8.9

(Continued and end)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2
Real total expenditure, monthly, average per person, growth, corresponding period of the previous year =100, %														
2005	-0.5	1.4	6.0	0.8	1.6	7.9	-4.2	2.8					2.3	3.4
2004	5.5	6.4	2.8	8.8	4.6	-0.4	11.3	5.5	9.2	3.2	6.2	-0.9	4.8	4.3
2003	12.4	3.3	8.3	8.9	3.1	7.3	7.9	3.7	0.1	4.3	3.1	1.9	8.0	6.4
Real cash expenditure, monthly, average per person, growth, corresponding period of the previous year =100, %														
2005	-0.4	1.9	6.8	2.3	2.9	9.0	-3.9	3.4					2.8	4.7
2004	5.8	7.2	3.3	9.8	5.4	1.1	13.9	6.9	10.9	5.2	8.7	3.3	5.4	5.4
2003	12.8	3.1	8.9	8.6	4.8	7.7	7.7	4.3	-0.4	4.6	3.4	5.9	8.2	7.0

1) Excluding credits to Monetary Financial Institutions.

2) Including credits to Non-financial Public Corporations.

3) Average monthly values by quarter are calculated as simple average of monthly per capita values.

Sources: Employment Agency, Bulgarian National Bank, Ministry of Finance, National Statistical Institute and own calculations.

Acronyms:

GDP = Gross domestic product

“ - “ = Not applicable or missing data

ANNEX 2: PROMULGATED REGULATORY DOCUMENTS

Regulatory Documents	Status	Official Gazette
ORDINANCE on free trade	New	No. 54 / 1.07.2005
EUROPE ASSOCIATION AGREEMENT between the European Communities and their Member States on one part and the Republic of Bulgaria on the other part	Amended/Supplemented	No. 54 / 1.07.2005
ORDINANCE on the capital adequacy of banks	Amended/Supplemented	No. 55 / 5.07.2005
GOVERNMENTAL REGULATION on specifying the role and functions of the national aid coordinator and his or her relationship with the program director/sector director in managing Community aid for Bulgaria under the pre-accession instruments PHARE and ISPA	New	No. 56 / 8.07.2005
RULES ON THE STRUCTURE of the Tourism Agency	Amended/Supplemented	No. 56 / 8.07.2005
RULES on the structure of the Ministry of Agriculture and Forestry	Amended/Supplemented	No. 56 / 8.07.2005
ORDINANCE on the terms and procedure of issuing import licenses for agricultural products within the tariff quotas	New	No. 56 / 8.07.2005
ORDINANCE on the terms and procedure of issuing visas	Amended/Supplemented	No. 56 / 8.07.2005
RULES on the structure and activity of the Anti-discrimination Commission	New	No. 57 / 12.07.2005
ORDINANCE on the terms and procedure of assessing the assets and liabilities of supplementary pension insurance funds and the pension insurance company, the value of fund's net assets for the purpose of calculating and quoting the value of one share, and on the requirements for keeping individual lots	Amended/Supplemented	No. 57 / 12.07.2005
ORDINANCE on the terms and procedure of classifying, packing and labeling chemical substances and preparations	Amended/Supplemented	No. 57 / 12.07.2005
GOVERNMENTAL DECREE on the approval of Tariff of charges for products generating mass waste after use	Amended/Supplemented	No. 58 / 15.07.2005
GOVERNMENTAL REGULATION on the approval of ordinance on the requirements for production and marketing of batteries and on the treatment and transportation of battery waste	New	No. 58 / 15.07.2005
RULES ON THE STRUCTURE of the Council of Ministers and its Administration	Amended/Supplemented	No. 58 / 15.07.2005
ORDINANCE on the requirements for production and marketing of batteries and on the treatment and transportation of battery waste	New	No. 58 / 15.07.2005
ORDINANCE on packages and package waste	Amended/Supplemented	No. 58 / 15.07.2005
RULES on the implementation of the Public Procurement Act	Amended/Supplemented	No. 59 / 19.07.2005
RULES on the structure and activities of the National Health Insurance Fund	Amended/Supplemented	No. 59 / 19.07.2005
ORDINANCE on awarding small public procurement contracts	Amended/Supplemented	No. 59 / 19.07.2005
ORDINANCE on the terms and procedure of transportation of radioactive substances	New	No. 60 / 22.07.2005
ORDINANCE on the terms and procedure of registration of local and imported tobacco products, trade in tobacco goods and trade control	Amended/Supplemented	No. 61 / 26.07.2005
ORDINANCE on the large exposures of banks	Amended/Supplemented	No. 62 / 29.07.2005
ORDINANCE on the assessment and classification of the risk exposures of banks and on making provisions for depreciation losses	Amended/Supplemented	No. 62 / 29.07.2005
ORDINANCE on consolidation-based supervision	Amended/Supplemented	No. 62 / 29.07.2005
ORDINANCE on assessment of the amount of investments of banks under Art. 30 of the Banks Act.	Amended/Supplemented	No. 62 / 29.07.2005
ORDINANCE on the registration of ports in the Republic of Bulgaria	New	No. 62 / 29.07.2005
ORDINANCE on the registration of port operators in the Republic of Bulgaria	New	No. 62 / 29.07.2005
ORDINANCE on the minimum required reserves maintained by banks with the Bulgarian National Bank	Amended/Supplemented	No. 62 / 29.07.2005
ACT on Foreigners in the Republic of Bulgaria	Amended/Supplemented	No. 63 / 2.08.2005
ORDINANCE on the rules and standards for the structure of the different types of territories and structural zones	Amended/Supplemented	No. 63 / 2.08.2005
ORDINANCE on the terms and procedure of the activity carried out by operators of the electricity system and distribution networks, by the on-duty operations staff of electricity sites and the electric appliances of consumers	Amended/Supplemented	No. 63 / 2.08.2005
ORDINANCE on the list of medicines for outpatient treatment which are fully or partially payable by the National Health Insurance Fund	Amended/Supplemented	No. 63 / 2.08.2005
INSTRUCTION on the implementation of the Ordinance on labor categorization upon retirement	Amended/Supplemented	No. 63 / 2.08.2005
2005 NATIONAL FRAMEWORK AGREEMENT between the National Health Insurance Fund and the Bulgarian Doctors Union and the Union of Dentists in Bulgaria	Amended/Supplemented	No. 63 / 2.08.2005
ORDINANCE on the rates of admissible emissions of harmful substances (pollutants) emitted to the air by sites and activities with stationary sources of emissions	New	No. 64 / 5.08.2005

ORDINANCE on the rates for admissible emissions (concentration in waste gases) of harmful substances emitted to the air by stationary sources	Amended/Supplemented	No. 64 / 5.08.2005
COMMERCIAL CODE	Amended/Supplemented	No. 66 / 12.08.2005
ORDINANCE on the terms and procedure of entry and deletion of public companies, other issuers of securities and securities issues in the register of the Financial Supervision Commission	New	No. 66 / 12.08.2005
Entries RULES	Amended/Supplemented	No. 67 / 16.08.2005
ACT on the storage of and trade in grain	Amended/Supplemented	No. 69 / 23.08.2005
Fodders ACT	Amended/Supplemented	No. 69 / 23.08.2005
RULES on the structure and activities of the Investors in Securities Compensation Fund	New	No. 69 / 23.08.2005
ORDINANCE on compliance marking	New	No. 69 / 23.08.2005
ORDINANCE on Industrial Property Representatives	Amended/Supplemented	No. 69 / 23.08.2005
ORDINANCE on the minimum requirements for the protection of the health and safety of workers against risks resulting from exposure to noise	New	No. 70 / 26.08.2005
ACT on the Bulgarian identity documents	Amended/Supplemented	No. 71 / 30.08.2005
Forestry ACT	Amended/Supplemented	No. 72 / 2.09.2005
ORDER of the Central Customs Directorate on improving customs control efficiency	Amended/Supplemented	No. 73 / 9.09.2005
ACT on copyright and neighboring rights	Amended/Supplemented	No. 74 / 13.09.2005
ACT on the administrative regulation of the production and trade in mirror disks, matrices and other carriers containing objects of copyright and neighboring rights	New	No. 74 / 13.09.2005
ACT on the protection against environmental noise	New	No. 74 / 13.09.2005
ACT on the registration and control of farm and forestry machines and equipment	Amended/Supplemented	No. 74 / 13.09.2005
Social Security CODE	Amended/Supplemented	No. 76 / 20.09.2005
Labor CODE	Amended/Supplemented	No. 76 / 20.09.2005
CRIMINAL CODE	Amended/Supplemented	No. 76 / 20.09.2005
ACT on the safe use of nuclear energy	Amended/Supplemented	No. 76 / 20.09.2005
Value Added Tax ACT	Amended/Supplemented	No. 76 / 20.09.2005
Health ACT	Amended/Supplemented	No. 76 / 20.09.2005
Health Insurance ACT	Amended/Supplemented	No. 76 / 20.09.2005
ACT on the health and safety at the workplace	Amended/Supplemented	No. 76 / 20.09.2005
Medical Institutions ACT	Amended/Supplemented	No. 76 / 20.09.2005
Merchant Shipping CODE	Amended/Supplemented	No. 77 / 27.09.2005
Waters ACT	Amended/Supplemented	No. 77 / 27.09.2005
ORDINANCE on the market access of air carriers	New	No. 77 / 27.09.2005
Structure of the Territory ACT	Amended/Supplemented	No. 77 / 27.09.2005
Waste Management ACT	Amended/Supplemented	No. 77 / 27.09.2005
ACT on the technical requirements for products	Amended/Supplemented	No. 77 / 27.09.2005
Environment Protection ACT	Amended/Supplemented	No. 77 / 27.09.2005
ACT on the independent financial audit	Amended/Supplemented	No. 77 / 27.09.2005
Railway Transport ACT	Amended/Supplemented	No. 77 / 27.09.2005
Telecommunications ACT	Amended/Supplemented	No. 77 / 27.09.2005
GOVERNMENTAL REGULATION on the set up of a Public Procurement Agency to the Minister of Economy and Energy and on the approval of Rules on the Structure of the Public Procurement Agency	Amended/Supplemented	No. 78 / 30.09.2005
GOVERNMENTAL REGULATION on the set up of a Council for Economic Policy	Amended/Supplemented	No. 78 / 30.09.2005
ORDINANCE on the technical rules and standards for the design, construction and operation of the sites and facilities for production, transfer and distribution of thermal energy	Amended/Supplemented	No. 78 / 30.09.2005
ORDINANCE on the designation and commercial presentation of wines, alcoholic beverages and grape and wine products	Amended/Supplemented	No. 78 / 30.09.2005
ORDINANCE on the procedure of carrying out trade in ferrous and non-ferrous metal waste	Amended/Supplemented	No. 78 / 30.09.2005
ORDINANCE on specifying the types of alcoholic beverages, the rules for their production, permitted additives and conditions for their use	Amended/Supplemented	No. 78 / 30.09.2005
ORDINANCE on the licensing of activities in the energy sector	Amended/Supplemented	No. 78 / 30.09.2005

ORDINANCE on the categorization of the railway lines in the Republic of Bulgaria included in the railway infrastructure and on the closing of individual lines or line sections	Amended/Supplemented	No. 78 / 30.09.2005
ORDINANCE on the quality requirements for liquid fuels and on the terms and procedure of their control	Amended/Supplemented	No. 78 / 30.09.2005
ORDINANCE on the labeling requirements for new passenger cars in terms of fuel consumption and carbon dioxide emissions	Amended/Supplemented	No. 78 / 30.09.2005
ORDINANCE on the labeling requirements for household appliances in terms of their noise emissions in the air	Amended/Supplemented	No. 78 / 30.09.2005
ORDINANCE on the labeling requirements for household appliances in terms of the consumption of electricity and other resources	Amended/Supplemented	No. 78 / 30.09.2005
ORDINANCE on the labeling and the names of textile products	Amended/Supplemented	No. 78 / 30.09.2005
ORDINANCE on the procedure of issuing licenses and permits for safe use of nuclear energy	Amended/Supplemented	No. 78 / 30.09.2005
ORDINANCE on the procedure assessment, collection, spending and control of funds and on the contributions payable to the Radioactive Waste Fund	Amended/Supplemented	No. 78 / 30.09.2005
ORDINANCE on the conditions to be satisfied by quality wines produced in designated regions and on the terms and procedure of their approval	Amended/Supplemented	No. 78 / 30.09.2005
ORDINANCE on the structure and safe operation of gas-transmission and gas-distribution pipelines and of natural gas facilities, installations and appliances	Amended/Supplemented	No. 78 / 30.09.2005.
ORDINANCE on the structure and safe operation of oil and oil product pipelines	Amended/Supplemented	No. 78 / 30.09.2005
ORDINANCE on the terms and procedure of issuing and withdrawing licenses for industrial tobacco processing and for production of tobacco goods	Amended/Supplemented	No. 78 / 30.09.2005
ORDINANCE on the terms and procedure of awarding special public procurement contracts	Amended/Supplemented	No. 78 / 30.09.2005
ORDINANCE on the terms and procedures of awarding activities under Article 7, paragraph 2 of the Small and Medium-sized Enterprises Act	Amended/Supplemented	No. 78 / 30.09.2005

A. GENERAL NOTES

The review of the Bulgarian economy is an authentic expert product of the Center for Economic Development, made possible mostly owing to the long experience of the Center in the field of applied studies of the economic policy and economic development of the country.

Structure of the report. The present report on the Bulgarian economy comprises:
(1) a summary of the report,
(2) economic analysis in 14 sectors described in detail in Topics and Sections,
(3) two annexes containing updated macroeconomic indicators and the regulatory documents promulgated in the review period,
(4) these methodological notes,
(5) English translation of the summary, and
(6) chronicle of CED's activity in the review period.

Review period. The report contains detailed presentation and assessment of the third quarter of 2005. Where necessary, significant events, facts and data of periods before 2005 have been highlighted. Where possible, data comparisons have been made against previous years. At many points also the short-term trend has been outlined.

Selection of Topics. The structure of the presentation above follows two principles simultaneously. First, the strive is towards giving a more comprehensive presentation of the subject matter areas, with corresponding prioritization of the range of matters discussed. Second, the different topics and analyses reflect the experience and interests of the experts from the Center for Economic Development.

Topics and Sections. The review of the Bulgarian economy starts with presentation of the *macroeconomic dynamics* discussed against the background of the following basic categories: GDP, foreign trade, foreign direct investments, inflation, employment and unemployment. After that, the annual values of the *Estat index of business climate* in Bulgaria *and NSI's monthly business surveys* are presented and compared. The national economic events in the review period, which have direct or indirect effect on the competitiveness of the Bulgarian enterprises, are analyzed in the section on the *enterprise policy*. Such events are described in the sub-sections on encouragement of entrepreneurship, investment promotion policy, access to finance, effectively functioning markets, commercial policy and preparation for the single European market, privatization and concessioning, regulatory regimes, public procurement regulation, public administration reform, combating corruption, index of economic freedom. In the specific Bulgarian economic environment, the enterprise policy has two basic aspects: (1) transformation, which is mostly associated with the process of privatization and liberalization of the economy, and (2) competitive orientation, which involves the policies to achieve economic growth and competitiveness of the Bulgarian enterprises. The corresponding section of the report studies problems concerning both aspects of the Bulgarian enterprise policy.

The *public finance* section covers the budget implementation and the fiscal reserve dynamics, the foreign and the domestic debt. The wide topic of *social and health policies* encompasses the issues of social security, employment and unemployment, labor market policy, incomes and social partnership. A review is made of the current problems and condition of the healthcare reform. The *environmental policy* is discussed both as a specific element of the economic policy and as a factor for the economic environment.

The financial sector is discussed by means of the *banking system* and the *capital market*. Then comes the review of a number of sectors of significant importance to the economic development of Bulgaria – *energy, transport, high technology and communications, tourism and agriculture*. The section on *regional policy* studies the political decisions, facts and events relating to the achievement of balanced and sustainable development of the regions and reduction of the disproportions between them, as well as the process of social and economic cohesion with the European Union.

The annexes at the end constitute an integral part of the presentation. *Annex 1* presents in detail the basic macroeconomic indicators. *Annex 2* contains the list of newly passed legislation and amendments to laws, which are of significant importance to the economic development of the country, and have been promulgated in the Official Gazette in the review period. Since 2005, this annex also contains a brief review of the more important legislative amendments in the respective quarter.

The work was finally completed on 15 October 2005.

B. SOURCES

Basic Sources. Statistical and other information and data from the sources below have been used in the analyses:
- National Assembly
- Council of Ministers
- Ministry of Energy and Energy Resources
- Ministry of Agriculture and Forestry
- Ministry of Economy
- Ministry of Transport and Communications
- Ministry of Labor and Social Policy
- Ministry of Finance
- National Statistical Institute
- National Social Security Institute
- Employment Agency
- Agency for Small and Medium-sized Enterprises

- Privatization Agency
- Bulgarian National Bank
- Bulgarian Stock Exchange – Sofia AD
- Financial Supervision Commission
- Delegation of the European Commission
- European Union
- Eurostat
- European Bank for Reconstruction and Development
- Organization for Economic Cooperation and Development
- World bank
- Official Gazette
- The periodical press

Additional Sources. We have also used the conclusions from a large number of own outputs and works, some of which are parts of assigned research projects, as well as analyses by other researchers. The particular sources and publications are quoted at the respective places in the text.

C. THE ESTAT INDEX OF BUSINESS CLIMATE IN BULGARIA

The business climate survey is based on own original methodology, developed by the team of the Agency for Social and Marketing Surveys Estat and the Center for Economic Development. The more significant details of the methodology are described below.

Methodology of the Sample. The survey is conducted on a quarterly basis among the managers of some 400 companies. The sample is a two-level panel one (at the first level the companies are divided into groups by regions, and at the second level – according to their economic sectors as per nomenclature A6 of the NSI), and it is grouped on the basis of the indices “number of employees” and “type of ownership”. The sample is a guaranteed representative one at the level of going concerns.

Methodology of the Registration. The information has been collected using the method of an inquiry at the work place. The interviews were held with the owners of the companies covered by the sample, or with persons authorized to make management decisions and to sign financial statement documents (managers, chief accountants, commercial or marketing directors).

Questionnaire Content. The questionnaire contains eight substantive questions and three passport questions. The integrated index is comprised of three basic components. The questions from one to five inclusive comprise Component I – “General Condition of the Company”; question six – Component II – “Investment Attitudes and Corporate Strategies”; questions seven and eight – Component III – “Business Environment”.

Index Calculation: (1) preliminary preparation. The preliminary preparation includes weighting of the data according to the indicators “economic sector” and “number of employees”, recoding and calculating values for the respective questions.

- Questions with one possible answer – the original scales are of Likert type with codes from 1 (the highest degree) to 5 (the lowest degree). Recoding is done so as to have a scale from -2 (the lowest degree) to +2 (the highest degree).
- Multiple-choice questions – these questions are recoded in advance so that possible answers are located symmetrically on both sides of the neutral point (the zero).

Index Calculation: (2) components. The index for each component, which comprises an indicator question, is calculated as a weighted average value. Weights are assigned to each indicator within a component by means of expert evaluation. The value for each component (“General Condition of the Company”; “Investment Attitudes and Corporate Strategies”; “Business Environment”) is calculated as a weighted average.

Index Calculation: (3) integrated index. The integrated index is calculated as a weighted average of the three basic components mentioned above. The weight for each of the components is determined by means of expert evaluation.

Index Values. The Estat index of business climate assumes values from -100 to +100. The business climate condition is assessed according to the following scale, similar to the one used in the German IFO Business Climate Index:

-100	to -61	very poor
-60	to -21	poor
-20	to +20	average
+21	to +60	good
+6	to +100	very good

Index Interpretation. The integrated index, as well as the three basic components assume values within the interval [-100, +100]. The set of tools allows determining also the direction of the index. The difference between the values of questions Q3 (assessment of the expected condition), Q2 (assessment of the condition at a certain point in time) and Q1 (assessment of the condition during the preceding period) is applied as a criterion for determining the direction.

Additional Notes. Beside everything aforesaid about the methodology, in many places throughout the text additional methodological and other notes and comments are given.

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THE CENTER FOR ECONOMIC DEVELOPMENT IN THE PERIOD JULY – SEPTEMBER 2005

Project implemented by the center for economic development and the economics institute in Belgrade

The meeting at work, 28 September 2005.

In the period December 2004 – September 2005 CED expert team implemented in partnership with representatives of the Economics Institute in Belgrade a joint project on Present State and Future Perspectives of the Cross-border Cooperation between Bulgaria and Serbia on Economic Policy and EU Accession.

The project aimed to make a review and analysis of the real state of cooperation and partnership between NGOs from Serbia and from Bulgaria, to develop and propose a strategy for promoting partnerships between think tanks from Bulgaria and from Serbia on economic policy formulation and EU integration. The strategy aims at further involving the expert community, the academic circles and other interested groups in trans-border cooperation and in the process of restructuring, reforms and changes in the context of EU accession.

The Center for Economic Development and the Economics Institute in Belgrade are committed to assisting the integration processes in Serbia by promoting the dialogue between representatives of professional economic circles and the civil society about future tasks, possible risks and the need of public awareness and of a professional public debate on the realities and perspectives of EU accession. CED shared specific experience from recent years, which corresponded best to Serbia's current situation. The strategy for cross-border cooperation will help to develop a systematic approach in enhancing the capacities for trans-border cooperation between NGOs from Bulgaria and from Serbia and Montenegro. Cooperation among NGOs will help to involve

the other sectors in building effective partnerships towards promoting economic development and improving individual awareness of EU integration realities. This is an important aspect of the strategy since both partners note in their analyses that for various reasons the cross-border cooperation between Serbia and Bulgaria is undervalued and its European structure development potential has not been discussed. Project data will help to raise the awareness of NGOs about the real state of cross-border cooperation and about partnerships.
The strategy has been developed on basis of the analysis and conclusions about the real state of cross-border cooperation between Serbia and Bulgaria.

Partner meeting was organized in Sofia on 28 September 2005. Participants from CED included Mrs. Maria Prohaska, Director, Mrs. Marieta Tzvetkovska, Senior Expert and Mrs. Violeta Spassova, Expert. The Economics Institute was represented by Mrs. Elena Galic, Executive Director and by the experts Mr. Milan Kovac and Mr. Milan Pavlovic. Partners discussed and exchanged their views about the surveys and interviews conducted in NGOs from Serbia and Bulgaria and about the interest and commitment to promoting cooperation of the organizations included in the survey. Discussions focused on the analyses developed for Bulgaria and Serbia, followed by exchange of views and recommendations on how to reflect better partners' views about the real state of the NGO sector in Bulgaria and Serbia. Partners made detailed review of the proposed draft Cooperation Strategy, with respective refinements. A draft Action Plan was proposed and discussed during the meeting. It was decided for the final version of the Plan to be coordinated at work level.

It is expected for the strategy and the conclusions to be approved at a closing forum within Open Society Institute's European Integration and Regional Stability Program.

Global competitiveness report, 2005-2006

At the end of September 2005, the World Economic Forum presented the official results of the annual **global competitiveness report, 2005-2006**. The report is among the most comprehensive and representative surveys of the growth potential of economies worldwide.
Since 1998, the **Center for Economic Development** is an **official partner** of the Forum in collecting and processing information on Bulgaria.

The report provides a **ranking of countries in terms of their competitiveness**. Rankings are drawn from statistical information and economic opinion surveys conducted among business leaders from all countries in the survey.

The report is unique in terms of its methodology since it uses a combination of exact quantitative indicators and opinions and expectations of business leaders from all countries in the survey. It provides an analysis of the key determinants of the potential for economic growth. Particular attention is placed on macroeconomic environment, the quality of public institutions and the level of technological development. Highlighted are the competitive strengths and weaknesses of all surveyed economies.

Finland Tops the Ranking Again

Finland remains the most competitive economy in the world for the fourth year running. The county owes its strong performance to an excellent macroeconomic environment and good quality of public institutions. The other key factor for successful development is the high quality of corporate strategies and, primarily, the proactive corporate policy focused on new technologies and innovative solutions.

Nordic countries continue to do very well in the competitiveness rankings – they are in the top ten of the most competitive economies – Finland (1); Sweden (3); Denmark (4); Iceland (7); Norway (9).

Among other European states, the most notable developments include Ireland and Poland, which was ranked below Bulgaria last year. However, some progress in Poland's performance is visible with the country moving up 9 places to 51st.

Overall, many of the new accession countries show measured improvement in levels of competitiveness over recent years. This is due in large part to their efforts to implement good management practices and institutional reforms. Estonia continues to perform well, at the impressive 20th place, for the second year running. It is the most competitive economy among the ten counties recently acceding to the EU.

At the same time, some old EU members are dropping in the rankings. **Greece** fell to 46th place from 37th last year, **Italy** remained at number 47. These are the two worst performing economies among EU Member States. Major reasons for the poor performance of Greece include turbulent macroeconomic environment and pessimistic expectations of business leaders about mid-term country development.

The United States is the second most competitive country, the same as last year. The country's innovative development achievements are offset to some degree by its weaker performance in terms of macroeconomic environment, particularly public finance.

Southeast Asia countries traditionally perform well, notably **Taiwan** and **Singapore**, which are ranked 5th and 6th, respectively. **Hong Kong** dropped in the ranking because of deteriorated institutional and judicial system performance.

The Forum team continues to expand the geographic coverage of the report, which in 2005 assesses 117 countries (104 last year). New African states and former Soviet republics are included.

Bulgaria Improves Its Ranking, Though Slowly

Bulgaria is included in the global competitiveness report for the seventh year running. In 2005, it moved up one place from 59th to 58th. Turkey and Romania remain far lower in the ranking at 66th and 67th place respectively.

Bulgaria improves its performance in terms of **macroeconomic stability**, moving three places up in the ranking (to 51st from 54th last year. At the same time, the quality of public institutions indicator has deteriorated, due in large part to deteriorated assessments of country's judicial system operation (88th place of 117 countries).

Negative is also the country's performance in terms of organized crime spread and insufficient protection of intellectual property rights.

In the World Economic Forum reports, Bulgaria traditionally performs well in terms of **corruption spread** assessments. In recent years, the country usually occupies places around 30th. However, in the latest report it has fallen to 38th place.

Bulgaria performs rather well in terms of the **index of technological development**. Assessments of transfer and implementation of new technologies show improvement (up to 58th place from 62nd last year). A look at the **quantitative indicators** shows that the country registers good achievements in the number of telephone lines, the percentage of students in higher education institutions, the number of Internet users and Internet hosts.

Negative are the business assessments about the quality of research and development, university – business cooperation, the inadequate role of foreign investments towards introduction of advance technologies in production.

Bulgaria does not show improvement in terms of **business competitiveness** and its two basic components – corporate strategies and business environment. This makes questionable the preparedness of Bulgarian companies to cope with the competitive pressure in the EU.

Assessments are good for the quality of education in exact sciences and mathematics and the availability of qualified engineers and technicians, which precondition innovative business development.

Assessments are negative for the infrastructure, which does not contribute to successful business development.

Notable for **corporate strategies** is the lack of experience and professionalism in company management and the lack of proactive personnel training and retraining policy (the unenviable 87th place).

Bulgaria performs well in terms of labor market flexibility, productivity – wage relation, equal treatment of women on the labor market, access to loans.

There are problems in environment protection and preserving the ecological balance.

MEETINGS "ON THE ROOF"

DISCUSSION ON INTERNATIONAL MIGRATION STATISTICS

A working meeting on statistics of international migration was organized on 6 July 2005 in the Roof Hall between the CED team of experts and two leading experts in the field from NSI – Mr. Ivan Balev, Director, Demographic and Social Statistics Division, and Mr. Jordan Kalchev, Head of Population Statistics Department. The meeting was initiated by CED based on a study of the relation between emigration and unemployment. The CED team presumes that growth in labor migration along with growth in employment on the Bulgarian labor market is a key factor for the fast decrease of unemployment in recent years with continuing effect in future years. However, the lack of regular and comparable statistics about international migration is a major problem in analyzing the relation between international migration and some basic demographic and socioeconomic phenomena and their parameters (for example, population number and structure, labor force number and structure).

The experts from NSI made a brief review of the long history of international migration statistics in Bulgaria and presented to CED experts NSI's current projects and problems concerning the regular statistical study of international migration. Within the international cooperation along EUROSTAT lines, NSI knows and can apply the international statistical experience and recommendations on international migration measurement, but the institution still strives towards improved collaboration from the other government institutions concerned for adoption in their work of the international definitions and criteria of submitting information about the movement of people across national borders.

Being an active user of statistical information, CED intends to continue its initiatives on the issue and is ready to organize a round-table discussion on International Migration with representatives of concerned government institutions. The idea behind this meeting is to discuss pragmatic approaches to enhance interdepartmental cooperation on the information support of international migration statistics.

PLEASE VISIT THE CED INTERNET PORTALS:

econ.bg
the business portal

stat.bg
the statistical portal

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